

# Legitimate expectations in investment treaty law: Understanding the roots and the limits of a controversial concept

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## I. Introduction

If one observes the awards given by investment treaty tribunals in the last few years, one will hardly find any example where the concept of ‘legitimate expectations’ has not been invoked by the claimant and, at least to a certain extent, endorsed by the arbitral tribunal. To transpose into the investment arbitration context the observation made by Lord Scott on the growing importance of the doctrine of legitimate expectations in English law, legitimate expectations are nowadays ‘much in vogue’.<sup>1</sup> Yet, despite the fortune that legitimate expectations seem to have been enjoying lately, there has been very little attempt by arbitral tribunals to provide a systematic and rigorous framework for the consideration of such expectations in investment treaty arbitration. Arbitral tribunals usually shy away from enquiring into the origins and the legal basis that justify the application of such concept and have typically taken for granted the idea that a breach of the investor’s expectations may be relevant in deciding upon

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<sup>1</sup> *EB (Kosovo) v. Secretary of State for the Home Department* [2008] UKHL 41, para. 31 *per* Lord Scott.

a violation of an investment treaty (especially of the fair and equitable treatment standard).

The purpose of this paper is to attempt to investigate the roots of the notion of legitimate expectations, and to examine to what extent the use of this concept is justified and appropriate within the investment treaty context. The paper starts by setting out certain methodological remarks which appear necessary to proceed with the exploration of the topic (Part II). As will be seen, the lack of a rigorous analysis by arbitral tribunal supporting the use of legitimate expectations characterizes the majority of investment treaty awards. With the possible exception of certain recent decisions (particularly in three Argentine cases – *Continental*, *Total*, and *El Paso*), which have attempted to provide a more thorough methodological contribution to the debate in this area, invocation of legitimate expectations has largely been founded on precedent, that is, awards citing to previous awards that have referred to the concept. This approach, without further elaboration, proves however unsatisfactory. This paper considers whether the notion of legitimate expectations may be rooted in principles of domestic administrative law that are common to a number of different legal systems, and whether, as a result of such commonalities, resort to general principles of law may offer a useful framework for the analysis in this area. To this end, Part III of the paper provides an overview of the domestic law systems that afford some form of protection to the individual's legitimate expectations arising out of the decision-maker's conduct. Part IV then turns to the investment treaty context, where recognition of legitimate expectations has generally been broader than in domestic legal systems. The paper will focus on protection of legitimate expectations under the fair and equitable treatment standard, in the context of which case law is by now quite rich. This paper seeks to contribute to the study of the topic by way of attempting to distil a system from the abundant and disordered jurisprudence on the issue. It will identify patterns of governmental conduct which tribunals have found to be susceptible of generating legitimate expectations deemed worthy of protection. In this regard, case law addresses mainly three types of different situations. In a first type of scenario, the state takes certain contractual commitments with the individual investor, which allegedly give rise to certain legitimate expectations (IV.2.A). In a second type of situation, characterized by a lower level of formality, we are merely in presence of what we could term 'unilateral declarations' by the host state (promises, assurances, representations, etc.). Do these types of acts also generate legitimate expectations which should be protected? And, if yes, what is the degree of specificity required to hold the state to its promises? (IV.2.B) Finally, in what is probably the most controversial scenario, a legitimate expectation of the investor is allegedly found to arise based on the existence of the regulatory framework *per se*, at the time the investor performs its investment in the host state. Here, to a greater extent than with regard to the other types of situations, the issue is closely linked to the concept of *change* – i.e., to what extent is the investor protected from a change in regulatory framework which affects its expectations? Or to what extent may it legitimately expect that the situation will remain unchanged? The issue is also related do the concept of *risk* – in what circumstances should a change in the regulatory framework (or the presence of an unstable framework) be considered part of the business risk that the investor has to bear when it chooses to invest in a particular country? (IV.2.C) Further, the role of the investor's conduct is also essential in

examining whether the expectations can be considered ‘reasonable’ (IV.3). Finally, the paper will draw some concluding remarks (V).

## II. In search of a justification beyond arbitral precedent

Little justification has generally been provided in arbitral awards to account for the use of legitimate expectations in the context of the fair and equitable treatment standard. This may seem quite surprising considering that the concept has no explicit anchoring in the text of the applicable investment treaties.<sup>2</sup> One dissenting arbitrator in a recent case observed that ‘the assertion that fair and equitable treatment includes an obligation to satisfy or not to frustrate the legitimate expectations of the investor [...] does not correspond, in any language, to the ordinary meaning to be given to the terms “fair and equitable”’.<sup>3</sup> The technique that has been used by most arbitral tribunals to buttress the application of the legitimate expectation principle is to simply refer to previous arbitral awards which have endorsed such concept, in a sort of cascade effect. Anthea Roberts’ observation that investment treaty jurisprudence generally resembles ‘a house of cards built largely by reference to other tribunal awards and academic opinions, with little consideration of the view and practices of states in general or the treaty parties in particular’<sup>4</sup> could probably find no better illustration than with regard to recurrent arbitral reference to the investor’s legitimate expectations. It is undeniable that there is now a line of cases (an ‘overwhelming trend’,<sup>5</sup> in the words of the *El Paso* tribunal) to the effect that legitimate expectations enjoy protection under the relevant investment treaty (although, as will be seen, case law in this regard is not always consistent). And once a few awards begin to endorse a certain idea, subsequent tribunals feel they have a ‘duty to adopt solutions established in a series of consistent cases’, with a view to ‘meet[ing] *the legitimate expectations* of the community of States and investors towards

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<sup>2</sup> Only certain investment treaties (mainly concluded by the U.S. and Canada) refer to ‘investment-backed expectations’ amongst the factors to be considered in order to determine whether a certain state measure constitutes indirect expropriation. See, e.g., U.S. Model BIT of 2012, Annex B(4)(a)(ii) (requiring, for a finding of indirect expropriation, consideration of ‘the extent to which the government action interferes with distinct, reasonable investment-backed expectations’). Similar language is found in the Canada Model BIT of 2003, Annex B.13(1)(b)(ii). These provisions are not considered in this paper, which focuses solely on fair and equitable treatment.

<sup>3</sup> *Suez et al. v. Argentina*, ICSID Case No. ARB/03/17, Decision on Liability, 30 July 2010, Separate Opinion of Arbitrator Pedro Nikken, para. 3. See also *id.*, paras. 20-21. See also the admonitions by the *ad hoc* committees in *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Chile*, ICSID Case No. ARB/01/7, Decision on Annulment, 21 March 2007, para. 67 (‘The obligations of the host State towards foreign investors derive from the terms of the applicable investment treaty and not from any set of expectations investors may have or claim to have. A tribunal which sought to generate from such expectations a set of rights different from those contained in or enforceable under the BIT might well exceed its powers, and if the difference were material might do so manifestly’), and *CMS Gas Transmission Company v. Argentina*, ICSID Case No. ARB/01/08, Decision on Annulment, 25 September 2007, para. 89 (‘Although legitimate expectations might arise by reason of a course of dealing between the investor and the host State, these are not, as such, legal obligations’).

<sup>4</sup> Anthea Roberts, *Power and Persuasion in Investment Treaty Interpretation: The Dual Role of States*, 104 AJIL 179, 179 (2010).

<sup>5</sup> *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011, para. 348.

certainty of the rule of law'.<sup>6</sup> As Stephan Schill has remarked, 'arbitral jurisprudence, including on fair and equitable treatment, is a *source of expectations* investors and states develop regarding the future application of the standard principles of international investment law, even if arbitral precedent is not formally binding.'<sup>7</sup> Thus, consistency in case law would seem to strengthen 'expectations' (of a different kind from those that form the subject of this paper) in the principal users of investment arbitration (states and investors) towards the certainty of the rule of law. The significance of arbitral precedent as understood in investment treaty arbitration has become undeniable and is a fascinating issue of ongoing debate.<sup>8</sup> Yet, it is not the topic of this paper. The point that is relevant to underscore for the limited purpose of this paper is that through a mechanical and not thoroughly thought-through reference to previous awards, tribunals evade their duty to explain the roots, the exact contours and possible limits of the issue of protection of the investor's legitimate expectations under the applicable investment treaty.<sup>9</sup> Resort to 'precedent' should be no substitute for analysis – especially if such analysis is not to be found in the early awards on which subsequent tribunals rely.<sup>10</sup>

One may, for example, look at the *Tecmed* case, in which the tribunal was one of the first to refer, within its discussion of the fair and equitable treatment standard, to protection of legitimate expectations. In a *dictum* that was referred to by several subsequent tribunals with approval<sup>11</sup> (but which has not escaped

<sup>6</sup> Saipem S.p.A. v. Bangladesh, ICSID Case No. ARB/05/07, Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007, para. 67 (emphasis added). In similar terms, see Duke Energy Electroquil Partners and Electroquil SA v. Ecuador, ICSID Case No. ARB/04/19, Award, 12 August 2008, para. 117; Burlington Resources Inc. v. Ecuador, ICSID Case No. ARB/08/5, Decision on Jurisdiction, 2 June 2010, para. 100 (noting arbitrator's Stern diverging view on this issue).

<sup>7</sup> Stephan Schill, *Fair and Equitable Treatment, the Rule of Law, and Comparative Public Law*, in INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW 151, 156-57 (Stephan Schill ed., 2010) (emphasis added).

<sup>8</sup> See, e.g., Gabriele Kaufmann-Kohler, *Arbitral Precedent: Dream, Necessity or Excuse?*, 23 ARB. INT'L 357 (2007); Christoph Schreuer & Matthew Weiniger, *A Doctrine of Precedent?* in THE OXFORD HANDBOOK OF INTERNATIONAL INVESTMENT LAW 1188 (Peter Muchlinski, Federico Ortino, & Christoph Schreuer eds., 2008); Tai-Heng Cheng, *Precedent and Control in Investment Treaty Arbitration*, 30 FORDHAM INT'L L. J. 1014 (2007).

<sup>9</sup> See, e.g., Biwater Gauff (Tanzania) Ltd. v. Tanzania, ICSID Case No. ARB/05/22, Award, 18 July 2008, para. 602 (noting that '[t]he general standard of "fair and equitable treatment" [...] comprises a number of different components, which have been elaborated and developed in previous arbitrations in response to specific fact situations. [...] these separate components may be distilled as follows: - Protection of legitimate expectations [...]') (emphasis added; internal footnotes omitted); International Thunderbird Gaming Corporation v. Mexico, NAFTA/UNCITRAL, Award, 26 January 2006, Separate Opinion Thomas Wälde, para. 30 (observing that investment treaty awards 'may not have explained the doctrinal background of the [legitimate expectations] principle, its scope and contours specifically, but these authoritative precedents have contributed towards establishing the "legitimate expectation" as a sub-category of "fair and equitable treatment" in the for this dispute here most pertinent investment treaties [...]').

<sup>10</sup> See also Elizabeth Snodgrass, *Protecting Investors' Legitimate Expectations – Recognizing and Delimiting a General Principle*, 21 ICSID REV. - FOREIGN INV. L.J. 1, 11 (2006).

<sup>11</sup> See, amongst many, LG&E Energy Corp et al. v. Argentina, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006, para. 127; MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Chile, ICSID Case No. ARB/01/7, Award, 25 May 2004, para. 114; Occidental Exploration and Production Company v. Ecuador, UNCITRAL/LCIA Case No. UN 3467, Final Award, 1 July 2004, para. 185; CMS Gas Transmission Company v. Argentina, ICSID Case No.

criticism),<sup>12</sup> the tribunal in that case tied fair and equitable treatment to ‘the good faith principle established by international law’ and thus concluded that fair and equitable treatment required ‘the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment.’<sup>13</sup> Yet, the tribunal cited no authority which would support the inclusion of protection of ‘basic expectations’ in the fair and equitable treatment standard. The tribunal’s reference to good faith can hardly serve that purpose. Despite being ‘one of the basic principles governing the creation and performance of legal obligations’, good faith may not provide a source of obligation in itself,<sup>14</sup> and more importantly does not suffice to explain why a treaty standard such as fair and equitable treatment should be read as encompassing the particular sub-element of the duty to protect legitimate expectations, at least not without further elaboration.

It is submitted that a more fruitful way to understand the provenance of legitimate expectations in the sense that is recurrent in investment treaty arbitration could rather be found in certain principles of domestic administrative law that are common to a number of legal systems. A claimant investor may effectively look at such domestic systems with a view to invoking a general principle of law within the meaning of Art. 38(1)(c) of the International Court of Justice (ICJ) Statute.<sup>15</sup> The relevance of general principles in investment treaty arbitration may be twofold.

First, general principles may be part of the applicable law. In an ICSID arbitration, for example, Art. 42 of the ICSID Convention dealing with the applicable law, refers to ‘such rules of international law as may be applicable’, which is to be read as including principles of law.<sup>16</sup> Also in those instances where an applicable law clause is included in a BIT, the treaty usually adopts a formulation referring to ‘international law’ (typically in combination with domestic law), which is clearly inclusive of general principles of law.<sup>17</sup>

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ARB/01/08, Award, 12 May 2005, para. 279; *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Award, 28 September 2007, para. 298.

<sup>12</sup> See *infra* at IV.1.

<sup>13</sup> *Técnicas Medioambientales Tecmed, S.A. v. Mexico*, ICSID Case No. ARB(AF)/00/2, Award, 29 May 2003, para. 154.

<sup>14</sup> See *Border and Transborder Armed Actions (Nicar. v. Hond.)*, 1988 I.C.J. 69, 105, para. 94 (Dec. 20) (‘The principle of good faith is, as the Court has observed, “one of the basic principles governing the creation and performance of legal obligations” (*Nuclear Tests*, I.C.J. Reports 1974, p. 268, para. 46; p. 473, para. 49); it is not in itself a source of obligation where none would otherwise exist’).

<sup>15</sup> See also Elizabeth Snodgrass, *Protecting Investors’ Legitimate Expectations – Recognizing and Delimiting a General Principle*, 21 ICSID REV. - FOREIGN INV. L.J. 1, 3 (2006) (general principles are ‘an appropriate and attractive intellectual framework for analyzing the concept of protection for investors’ legitimate expectations emerging in recent investment treaty arbitrations’).

<sup>16</sup> See CHRISTOPH H. SCHREUER, WITH LORETTA MALINTOPPI, AUGUST REINISCH, & ANTHONY SINCLAIR, *THE ICSID CONVENTION: A COMMENTARY* 607-610 (2d ed. 2009). See also Report of the Executive Directors of the International Bank for Reconstruction and Development on the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, para. 40, available at <http://icsid.worldbank.org>.

<sup>17</sup> See Tarcisio Gazzini, *General Principles of Law in the Field of Foreign Investment*, 10 J. WORLD INVESTMENT & TRADE 103, 112 (2009) (providing examples of applicable law clauses in BITs).



Second, general principles may inform (and have in fact informed) the interpretation or application of the fair and equitable treatment, which can be seen as ‘the perfect laboratory’ for the operation of such principles.<sup>18</sup> The idea that investment law may benefit from an approach based on comparative public law has found support in scholarly work,<sup>19</sup> and in certain recent awards.<sup>20</sup> Also a number of investment treaties or treaty models now expressly recognise that domestic law concepts having the status of general principles inform the content of investment protection standards, in particular the vaguely worded fair and equitable treatment standard.<sup>21</sup>

With specific regard to legitimate expectations, Thomas Wälde’s Separate Opinion in the *Thunderbird v. Mexico* case laid the groundwork for such a comparative public law inquiry.<sup>22</sup> Ideally carrying forward this type of examination, the arbitral tribunal in *Total v. Argentina* more recently found that ‘a comparative analysis of the protection of legitimate expectations in domestic jurisdictions is justified’.<sup>23</sup> The arbitral tribunal, however, appeared rightly mindful to stress that the principle of legitimate expectations has found recognition ‘both in civil law and in common law jurisdictions *within well defined*

<sup>18</sup> See Tarcisio Gazzini, *General Principles of Law in the Field of Foreign Investment*, 10 J. WORLD INVESTMENT & TRADE 103, 112 (2009). See also CAMPBELL MCLACHLAN, LAURENCE SHORE & MATTHEW WEINIGER, INTERNATIONAL INVESTMENT ARBITRATION. SUBSTANTIVE PRINCIPLES 259 (2007) (noting that the term fair and equitable treatment is ‘expressive of “general principles of law common to civilised nations”, within the meaning of Article 38(1)(c) of the Statute of the International Court of Justice’); ROLAND KLÄGER, ‘FAIR AND EQUITABLE TREATMENT’ IN INTERNATIONAL INVESTMENT LAW 271-273 (2011).

<sup>19</sup> See in particular INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW (Stephan Schill ed., 2010). See also Francisco Orrego Vicuña, *Foreign Investment Law: How Customary is Custom?*, in 99 Am. Soc’y Int’l. L. Proc. 97, 99-100 (2005) (‘[...] in the light of a number of recent decisions, “fair and equitable treatment” is not really different from the legitimate expectations doctrine as developed, for example, by the English courts and also recently by the World Bank Administrative Tribunal. International law is not unaware of major domestic legal developments, particularly when the rights of citizens are entangled in promises made by their governments and the citizens have in good faith relied upon them. Whether this standard may be developed beyond foreign investments or international administrative law is just a question of time. The common standard thus continues to evolve’).

<sup>20</sup> *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 111 (‘a comparative analysis of what is considered generally fair or unfair conduct by domestic public authorities in respect of private firms and investors in domestic law may also be relevant to identify the legal standards under BITs’). This passage was quoted with approval by the tribunal in *Toto Construzioni Generali S.p.A. v. Lebanon*, ICSID Case No. ARB/07/12, Award, 7 June 2012, para. 166, which added that ‘[t]he fair and equitable treatment standard of international law does not depend on the perception of the frustrated investor, but should use public international law and comparative domestic public law as a benchmark’.

<sup>21</sup> See U.S. Model BIT of 2004 (on which all subsequent U.S. BITs and FTAs with an investment chapter are modelled), and U.S. Model BIT of 2012, Art. 5(2)(a) (defining fair and equitable treatment as including ‘the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings *in accordance with the principle of due process embodied in the principal legal systems of the world*’, emphasis added); China-New Zealand FTA (2008), Art. 143, available at <http://www.chinafta.govt.nz> (‘Fair and equitable treatment includes the obligation to ensure that, *having regard to general principles of law*, investors are not denied justice or treated unfairly or inequitably in any legal or administrative proceeding affecting the investments of the investor’, emphasis added).

<sup>22</sup> *International Thunderbird Gaming Corporation v. Mexico*, NAFTA/UNCITRAL, Award, 26 January 2006, Separate Opinion Thomas Wälde, paras. 27-30.

<sup>23</sup> *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 128.

*limits*'.<sup>24</sup> Resort to comparativism may thus be indeed a valuable approach, provided, however, the relevant legal concepts (such as legitimate expectations) are imported with a clear understanding of their exact contours in the domestic systems of origin. With this comparative public law approach in mind, the paper now turns to examining protection of legitimate expectations under domestic legal systems.

### III. Protection of legitimate expectations in domestic legal systems: A general principle of law?

As several studies devoted to this topic have highlighted, a number of domestic legal systems protect legitimate expectations,<sup>25</sup> intended as 'the entitlement of an individual to legal protection from harm caused by a public authority resiling from a previous publicly stated position, whether that be in the form of a formal decision or in the form of a representation'.<sup>26</sup>

The reasons for protecting legitimate expectations are usually found to lie in a series of considerations. On the one hand, the disappointment by the decision-maker of an expectation may cause considerable harm to an individual who has relied upon its fulfilment (*the reliance theory*).<sup>27</sup> On the other hand, expectations are a central aspect of legal certainty and therefore of individual autonomy (*the rule of law theory*).<sup>28</sup> Under this second aspect, legal certainty and the individuals' capability to foresee the consequences of their actions are a prerequisite for rational enterprise in a capitalist economy.<sup>29</sup>

In German law, protection of legitimate expectations is linked to the fundamental principle of *Vertrauensschutz* (protection of trust), and its scope is particularly wide-reaching.<sup>30</sup> The German position has likely influenced the

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<sup>24</sup> Id. (emphasis added).

<sup>25</sup> See generally SØREN SCHØNBERG, LEGITIMATE EXPECTATIONS IN ADMINISTRATIVE LAW (2000).

<sup>26</sup> Chester Brown, *The Protection of Legitimate Expectations as a "General Principle of Law": Some Preliminary Thoughts*, 6(1) TRANSNATIONAL DISPUTE MANAGEMENT 2 (March 2009).

<sup>27</sup> SØREN SCHØNBERG, LEGITIMATE EXPECTATIONS IN ADMINISTRATIVE LAW 9-11 (2000).

<sup>28</sup> Id., at 12-24.

<sup>29</sup> Id., at 12 (quoting Max Weber's writings). See also, in the investment treaty context, *Suez et al. v. Argentina*, ICSID Case No. ARB/03/17, Decision on Liability, 30 July 2010, para. 203 ('reasonable and legitimate expectations are important factors that influence initial investment decisions and afterwards the manner in which the investment is to be managed. The theoretical basis of this approach no doubt is found in the work of the eminent scholar Max Weber, who advanced the idea that one of the main contributions of law to any social system is to make economic life more calculable and also argued that capitalism arose in Europe because European law demonstrated a high degree of "calculability." An investor's expectations, created by law of a host country, are in effect calculations about the future', internal footnote omitted).

<sup>30</sup> Chester Brown, *The Protection of Legitimate Expectations as a "General Principle of Law": Some Preliminary Thoughts*, 6(1) TRANSNATIONAL DISPUTE MANAGEMENT 5 (March 2009). See in particular § 38 of the German Law of Administrative Procedure ('Assurance. A promise made by a competent authority to take or refrain from taking an administrative act (assurance) must be in writing to be effective'), quoted in Hector A. Mairal, *Legitimate Expectations and Informal Administrative Representations*, in INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW 413, 416 (Stephan Schill ed., 2010). See also Christopher Forsyth, *The Provenance and Protection of Legitimate Expectations*, 47 CAMBRIDGE L.J. 238, 242-44 (1988); Georg Nolte, *General Principles of German and European Administrative Law – A Comparison in Historical Perspective*, 57(2) M.L.R. 191 (1994).

development of the principle in EU law,<sup>31</sup> where it is considered a general principle of EU law.<sup>32</sup> In the EU context, the doctrine has particular prominence in the context of retroactive application of laws.<sup>33</sup> Besides that, when representations of the Community institutions are at stake, a legitimate expectation may also arise, if it is the result of *precise and specific assurances* given by the administration.<sup>34</sup> In contrast, with regard to claims of stability of the regulatory system, protection of legitimate expectations does not allow a company to claim ‘a vested right to the maintenance of an advantage which it obtained from the establishment of the common organization of the market and which it enjoyed at a given time’.<sup>35</sup> The case law of the European Court of Justice (ECJ) is settled to the effect that ‘traders cannot have a legitimate expectation that an existing situation which is capable of being altered by the Community institutions in the exercise of their discretionary power will be maintained’.<sup>36</sup>

Despite the clear recognition of the doctrine as a general principle of EU law, the situation is not completely uniform in the domestic legal systems of the European member states. In France, the principle has not gained acceptance as part of French administrative law (except in situations which fall within the scope

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<sup>31</sup> Christopher Forsyth, *The Provenance and Protection of Legitimate Expectations*, 47 CAMBRIDGE L.J. 238, 242 (1988).

<sup>32</sup> See, amongst many, *VEMW et al. v. Directeur van de Dienst uitvoering en toezicht energie*, C-7/03, 7 June 2005, para. 73 (‘The principle of the protection of legitimate expectations is unquestionably one of the fundamental principles of the Community’). See also Stefán M. Stefánsson, *Legitimate Expectations in EC/EEA Law*, in *ECONOMIC LAW AND JUSTICE IN TIMES OF GLOBALISATION – WIRTSCHAFTSRECHT UND JUSTIZ IN ZEITEN DER GLOBALISIERUNG: FESTSCHRIFT FOR CARL BAUDENBACHER* 627, 628 (Mario Monti et al. eds., 2007) (‘the principle of legitimate expectations can not only be invoked as a rule of interpretation but also as an independent source of subjective rights’).

<sup>33</sup> TAKIS TRIDIMAS, *THE GENERAL PRINCIPLES OF EU LAW* 252-273 (2006, 2d ed.); PAUL CRAIG, *EU ADMINISTRATIVE LAW* 608-610 (2006).

<sup>34</sup> TAKIS TRIDIMAS, *THE GENERAL PRINCIPLES OF EU LAW* 281 (2006, 2d ed.). See, e.g., *Kyowa Hakko v. Commission*, Case T-223/00, 9 July 2003, [2003] ECR II-2553, para. 38 (‘a person may not plead infringement of the principle [of legitimate expectations] unless he has been given precise assurances by the administration’); *Van den Bergh v. Commission*, Case T-65/98, [2003] ECR II-4653, 23 October 2003, paras. 192-194. It has been noted that it is the ‘precise and specific’ hurdle ‘that applicants have found difficult to surmount, since the Community courts will not readily find that this criterion has been met’ (PAUL CRAIG, *EU ADMINISTRATIVE LAW* 628 (2006)).

<sup>35</sup> *Eridania v. Minister of Agriculture and Forestry*, Case 230/78, 27 September 1979 [1979] ECR 2749, paras. 21-22; *Werner Faust v. Commission*, Case 52/81, 28 October 1982, [1982] ECR 3745, 3762-63, paras. 26-27. See TAKIS TRIDIMAS, *THE GENERAL PRINCIPLES OF EU LAW* 269-271 (2006, 2d ed.). But see the milk quota cases, where Community legislation encouraging traders to take steps recommended by the Community institutions was found to give rise to legitimate expectations in situations not foreseen by the traders. See *Georg von Deetzen v. Hauptzollamt Hamburg-Jonas*, C-170/89, 28 April 1988, [1988] ECR 2355, paras. 10-16; *Mulder v. Minister van Landbouw en Visserij*, Case 120/86, 28 April 1998, [1988] ECR 2321, paras. 21-27. Tridimas explains that in these cases, legislation directed a Community institution to take into account a specific, well defined, interest. See TAKIS TRIDIMAS, *THE GENERAL PRINCIPLES OF EU LAW* 273-280 (2006, 2d ed.). According to PAUL CRAIG, *EU ADMINISTRATIVE LAW* 637-639 (2006), in cases of changes of policy, a legitimate expectation may arise only if the applicant is ‘able to point either to a bargain of some form between the individual and the authorities, or to a course of conduct or assurance on the part of the authorities which can be said to generate the legitimate expectation’.

<sup>36</sup> *Kyowa Hakko v. Commission*, Case T-223/00, 9 July 2003, [2003] ECR II-2553, para. 39.



of EU law).<sup>37</sup> Yet, it is argued that similar protection is nonetheless achieved by way of other principles, such as the right to be heard, the protection of vested rights, and legal certainty.<sup>38</sup>

In England, discussions on legitimate expectations have been engaging scholars and courts for many years.<sup>39</sup> Traditionally, English law provided only *procedural* protection of expectations. To say that protection granted to those who have seen their expectations defeated by an administrative decision is procedural means that the decision is set aside in order to give an opportunity to the individual to state its case, by allowing a hearing or adequate notice.<sup>40</sup> When the protection is *substantive*, the decision is definitely set aside (and thus the individual achieves what was expected as a matter of substance) or, in other cases, it is maintained but compensatory damages are awarded.<sup>41</sup> It is clear that only the second type of protection (in particular compensatory remedy for breach of substantive expectations) would be of interest for the purpose of an investment treaty claim.

To illustrate the distinction with an example, let us assume that an investor operating in the tobacco business, encouraged by a governmental grant, decides to build an oral snuff factory. Some years later, the government proceeds to ban oral snuff entirely. To protect the company's legitimate expectations as a matter of substance would imply quashing the ban or awarding compensation for the damages suffered. To protect expectations only procedurally, as the English court did in *R v. Secretary of State for Health, ex parte US Tobacco International Inc.*,<sup>42</sup> means to deny that the company's financial interest would override the interest in public health,<sup>43</sup> and to merely recognize that the company should have been granted an opportunity to comment on the scientific evidence on which the ban

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<sup>37</sup> See Elizabeth Snodgrass, *Protecting Investors' Legitimate Expectations – Recognizing and Delimiting a General Principle*, 21 ICSID REV. - FOREIGN INV. L.J. 1, 27 (2006).

<sup>38</sup> Chester Brown, *The Protection of Legitimate Expectations as a "General Principle of Law": Some Preliminary Thoughts*, 6(1) TRANSNATIONAL DISPUTE MANAGEMENT 5 (March 2009).

<sup>39</sup> The first English case to mention legitimate expectations is *Schmidt v. Secretary of State for Home Affairs*, [1969] 2 Ch. 149. See Christopher Forsyth, *The Provenance and Protection of Legitimate Expectations*, 47 CAMBRIDGE L.J. 238 (1988).

<sup>40</sup> See Hector A. Mairal, *Legitimate Expectations and Informal Administrative Representations*, in INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW 413, 414 (Stephan Schill ed., 2010).

<sup>41</sup> *Id.* See also the definition given in one English leading case, *R (Niazi) v. Secretary of State for the Home Department* [2008] EWCA Civ 755, para. 32 ('A substantive legitimate expectation arises where the court allows a claim to enforce the continued enjoyment of the content — the substance — of an existing practice or policy, in the face of the decision-maker's ambition to change or abolish it').

<sup>42</sup> *R v. Secretary of State for Health, ex parte US Tobacco International Inc.* [1992] QB 353.

<sup>43</sup> *Id.*, 369 *per* Taylor L.J. ('[...] if the Secretary of State concluded on rational grounds that a policy change was required and oral snuff should be banned in the public interest, his discretion could not be fettered by moral obligations to the applicants deriving from his earlier favourable treatment of them. It would be absurd to suggest that some moral commitment to a single company should prevail over the public interest. Accordingly, although it is regrettable that the applicants were kept in the dark for so long about the recommendation of a ban, I do not consider their plea of legitimate expectation can be upheld'). See also *id.*, 372 *per* Morland J. ('[applicants] must have been aware that their expectations could never fetter the Secretary of State's duty to promote and safeguard the health of the public. That is a duty which must, in my judgment, override private commercial expectations and interests. The right of government to change its policy in the field of health must be unfettered').

was based.<sup>44</sup>

Development of substantive protection of expectations under English law has been slow and difficult.<sup>45</sup> Yet, after the landmark *Coughlan* case decided in 2000 by the English Court of Appeal, it is now recognized that legitimate expectations also attract substantive legal protection. In *Coughlan*, the Court of Appeal found that:

Where the court considers that a lawful promise or practice has induced a legitimate expectation of a *benefit which is substantive*, not simply procedural, authority now establishes that here too the court will in a proper case decide whether to frustrate the expectation is so unfair that to take a new and different course will amount to an abuse of power. Here, once the legitimacy of the expectation is established, the court will have the task of weighing the requirements of fairness against any overriding interest relied upon for the change of policy.<sup>46</sup>

Although it remains a highly contentious matter, substantive protection of legitimate expectations can now be said to be established also in English law.<sup>47</sup> However, judges have held that its operation remains confined to ‘exceptional situations’.<sup>48</sup> The reason for this is that courts are generally cautious in assuming a role through their judicial review which belongs to the administrative decision-maker. Doctrines such as not-fettering, separation of powers and deference towards the administration’s balancing of individual and public interests have the consequence of limiting the courts’ power to find in favour of parties demanding substantive protection of expectations. Thus, courts will intervene only if there is a very serious imbalance between a person’s reasonable expectation and the wider public interest in a decision which will disappoint it.<sup>49</sup> The balancing exercise is subject to a ‘low intensity review’ which applies generally to discretionary

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<sup>44</sup> *Id.*, 371 *per* Taylor L.J. (‘It may well be that, in the end, the decision reached by the Secretary of State may prove to be wise and in the public interest, but such a draconian step should not be taken unless procedural propriety has been observed and those most concerned have been treated fairly’).

<sup>45</sup> See Paul Craig, *Substantive Legitimate Expectations in Domestic and Community Law*, 55(2) CAMBRIDGE L.J. 289, 290 (1996) (noting that ‘[English] courts have had little difficulty in recognising the existence of procedural legitimate expectations, and have accepted that such expectations can be generated in a number of differing ways. They have, however, shown considerably more reluctance to accept substantive legitimate expectations as part of the law’). For the traditional position against recognition of substantive legitimate expectations, see, *e.g.*, *R. v. Secretary of State for Transport, ex parte Richmond-upon-Thames London Borough Council*, [1994] 1 W.L.R. 74, 93 (noting that recognition of substantive legitimate expectations ‘would impose an obvious and unacceptable fetter upon the power, and duty, of a responsible public authority to change its policy when it considered that that was required in fulfilment of its public responsibilities. In my judgment the law of legitimate expectation, where it is invoked in situations other than one where the expectation relied on is distinctly one of consultation, only goes so far as to say that there may arise conditions in which, if policy is to be changed, a specific person or class of persons affected must first be notified and given the right to be heard’).

<sup>46</sup> *R v. North and East Devon Health Authority, ex parte Coughlan* [2001] QB 213. See Paul Craig and Søren Schønberg, *Substantive Legitimate Expectations after Coughlan*, PUBLIC LAW 684 (2000).

<sup>47</sup> SØREN SCHØNBERG, LEGITIMATE EXPECTATIONS IN ADMINISTRATIVE LAW 108-114 (2000).

<sup>48</sup> *R (Niazi) v. Secretary of State for the Home Department* [2008] EWCA Civ 755, para. 41.

<sup>49</sup> SØREN SCHØNBERG, LEGITIMATE EXPECTATIONS IN ADMINISTRATIVE LAW 112 (2000).

decision-making in English law.<sup>50</sup> Further, in those cases where representations by the administration were at issue, courts have been careful to limit protection of expectations to situations where those promises or assurances were ‘clear, unambiguous, and devoid of relevant qualification’.<sup>51</sup> Moreover, English courts are still particularly reluctant to intervene when expectations are frustrated by general changes of policy (rather than by departure from an individualised assurance).<sup>52</sup> When a change of general policy is at issue, there has been almost a total denial of judicial protection.<sup>53</sup> In *Hargreaves*, the high hurdle was set that a legitimate expectation, created by previous policy, could be invoked only if it could be shown that the new policy was irrational, perverse or unreasonable.<sup>54</sup>

The English acceptance of protection of substantive expectations has not been, at least for the time being, followed by other Commonwealth jurisdictions. Both Canada<sup>55</sup> and Australia<sup>56</sup> have been so far reluctant to extend judicial protection in cases of frustration of substantive expectations, and have generally taken the view that expectations about the exercise of administrative powers may only give rise to procedural rights.

In Latin American countries, recognition of the principle appears to be at its infancy, and its scope is to date fairly limited.<sup>57</sup> Yet, it is not unknown. It is significant that the ICSID tribunal in *Total v. Argentina*, when undertaking its

<sup>50</sup> Id. The exact standard of review to be applied by courts is debated. See Paul Craig and Søren Schønberg, *Substantive Legitimate Expectations after Coughlan*, PUBLIC LAW 684, 690-700 (2000).

<sup>51</sup> SØREN SCHØNBERG, LEGITIMATE EXPECTATIONS IN ADMINISTRATIVE LAW 120 (2000) (with further references to case law). See also *R (Niazi) v. Secretary of State for the Home Department* [2008] EWCA Civ 755, paras. 43 (requiring ‘a specific undertaking, directed at a particular individual or group, by which the relevant policy’s continuance is assured’) and 46 (‘pressing and focussed nature of the kind of assurance required if a substantive legitimate expectation is to be upheld and enforced’).

<sup>52</sup> See SØREN SCHØNBERG, LEGITIMATE EXPECTATIONS IN ADMINISTRATIVE LAW 142-146, 149 (2000) (noting that ‘English courts are [...] very reluctant to interfere where legitimate expectations are disappointed as a result of general changes of policy’); Melanie Roberts, *Public Law Representations and Substantive Legitimate Expectations*, 64(1) M.L.R. 112, 117 (2001) (noting that ‘[t]he courts are going to be more prepared to intervene in cases where the applicant was given a promise. [...] Where policies are involved it is harder for the courts to sustain a substantive legitimate expectation claim as the courts must be careful that upholding such a claim based on an original policy does not lead to the fettering of policy’).

<sup>53</sup> SØREN SCHØNBERG, LEGITIMATE EXPECTATIONS IN ADMINISTRATIVE LAW 16 (2000).

<sup>54</sup> *R v. Secretary of State for the Home Department, ex parte Hargreaves* [1997] 1 WLR 906, 924. See also Richard Clayton, *Legitimate Expectations, Policy, and the Principle of Consistency*, 62(1) CAMBRIDGE L.J. 93 (2003).

<sup>55</sup> But see Trevor Zeyl, *Charting the Wrong Course: The Doctrine of Legitimate Expectations in Investment Treaty Law*, 49(1) ALBERTA LAW REVIEW 203, 214-15 (2011) (in Canada, when legitimate expectations arise they lead to a duty of procedural fairness/due process, not substantive review).

<sup>56</sup> Matthew Groves, *Substantive Legitimate Expectations in Australian Administrative Law*, 32 MELBOURNE UNIVERSITY LAW REVIEW 470 (2008) (noting that Australian courts have so far confined protection of expectations to the procedural sphere, and arguing that Australian constitutional principles would preclude any judicial enforcement of substantive legitimate expectations in the future).

<sup>57</sup> Hector A. Mairal, *Legitimate Expectations and Informal Administrative Representations*, in INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW 413, 416-417 (Stephan Schill ed., 2010) (noting that ‘in some countries of Latin America the doctrine is used principally – so far – to limit the revocation of formal administrative decisions that were held to have created rights in benefit of a private party’).

comparative public law inquiry, referred, *inter alia*, to an Argentine 1977 Supreme Court decision granting protection in a situation of frustration of legitimate expectations.<sup>58</sup>

Could one, in light of this comparative overview, say that substantive protection of legitimate expectations has achieved global recognition in domestic law systems? While universality of identical rules is not required to establish a general principle of law, a careful examination of at least the most representative legal systems is called for.<sup>59</sup> And as Schreuer reminds, ‘great care must be taken to establish [general principles of law] by inductive proof and not simply to assume or postulate their existence’.<sup>60</sup> The comparative analysis carried out shows that it may be difficult to provide a clear-cut answer to the question. It is certainly true that the growing *substantive* protection of expectations in jurisdictions (such as England), which have traditionally been hostile to it, is a significant development. Moreover, the principle is well-established in a number of other administrative systems (in the civil law, German and Dutch, for example), and has enjoyed clear, consistent, and relatively broad acceptance within a supra-national context, such as the EU. On the other hand, there are also examples of jurisdictions which are reluctant to embrace the concept, although it could, at least in some cases, be argued that equal protection is nonetheless achieved by way of other legal concepts. Despite these uncertainties, one could nonetheless conclude that to establish an at least emerging general principle of protection of legitimate expectations would not seem to be an unrealistic endeavour.<sup>61</sup> It is thus this general principle that will inform the content of fair and equitable treatment in investment treaty law. However, the above analysis has also shown that even where the doctrine is accepted on the domestic level, it is accompanied by clear limitations, which must be kept in mind when attempting to invoke the principle within the investment treaty arbitration context. In particular, most domestic systems tend to distinguish protection of expectations in situations of individualised representations which the administration repudiates, from cases where the individual is affected by a general change of policy. It is the first case that is treated as the strongest, whereas protection in the second instance would be quite exceptional, and would attract extremely restrained judicial review. For, as Craig explains, ‘an unequivocal representation made to a person [...] carries a particular moral force’ and ‘holding the public body to such a representation is less likely to have serious consequences for the administration as a whole.’<sup>62</sup>

With that background in mind, it is to investment treaty law that the article now turns. It will be seen that in the investment framework, invoking protection

<sup>58</sup> See *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, fn. 136.

<sup>59</sup> See Elizabeth Snodgrass, *Protecting Investors’ Legitimate Expectations – Recognizing and Delimiting a General Principle*, 21 ICSID REV. - FOREIGN INV. L.J. 1, 21-22 (2006) (arguing that ‘[i]n extrapolating a general principle of law from rules of municipal law one need not establish actual universality of application of identical rules’).

<sup>60</sup> CHRISTOPH H. SCHREUER, WITH LORETTA MALINTOPPI, AUGUST REINISCH, & ANTHONY SINCLAIR, *THE ICSID CONVENTION: A COMMENTARY* 610 (2d ed. 2009).

<sup>61</sup> For a contrary opinion, see Trevor Zeyl, *Charting the Wrong Course: The Doctrine of Legitimate Expectations in Investment Treaty Law*, 49(1) ALBERTA LAW REVIEW 203, 209 (2011) (‘recognizing substantive expectations as part of the general principles of law is at this point premature and amounts to a misstatement of a general principle of law’).

<sup>62</sup> PAUL CRAIG, *EU ADMINISTRATIVE LAW* 611 (2006)

of legitimate expectations has been generally easier than it has been in domestic or in the EU context.<sup>63</sup>

#### IV. Legitimate expectations and fair and equitable treatment

##### 1. General remarks

Although legitimate expectations are invoked also in the context of indirect expropriation, it is under the fair and equitable treatment standard that legitimate expectations have enjoyed more prominence and a safer chance of success.<sup>64</sup>

In his Separate Opinion in *Thunderbird v. Mexico*, Thomas Wälde analysed what he considered to be the origins, role and scope of the principle of legitimate expectations, and noted that there had been

[...] a significant growth in the role and scope of the legitimate expectation principle, from an earlier function as a subsidiary interpretative principle to reinforce a particular interpretative approach chosen, to its current role as a self-standing subcategory and independent basis for a claim under the “fair and equitable standard” as under Art. 1105 of the NAFTA. This is possibly related to the fact that it provides a more supple way of providing a remedy appropriate to the particular situation as compared to the more drastic determination and remedy inherent in concept of regulatory expropriation. It is probably partly for these reasons that “legitimate expectation” has become for tribunals a preferred way of providing protection to claimants in situations where the tests for a “regulatory taking” appear too difficult, complex and too easily assailable for reliance on a measure of subjective judgment.<sup>65</sup>

The first arbitral tribunal to clearly spell out that fair and equitable treatment encompasses protection of expectations was the tribunal in *Tecmed v. Mexico*, who understood the fair and equitable treatment clause in the Spain-Mexico Bilateral Investment Treaty (BIT) to ‘require[] the Contracting Parties to provide to international investments treatment that does not affect the basic expectations

<sup>63</sup> See TAKIS TRIDIMAS, *THE GENERAL PRINCIPLES OF EU LAW* 251 (2006, 2d ed.) (noting that ‘the overwhelming majority of claims based on breach of the [legitimate expectations] principle have been rejected’); Hector A. Mairal, *Legitimate Expectations and Informal Administrative Representations*, in *INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW* 413, 450 (Stephan Schill ed., 2010) (‘[i]n the national and EU systems, case law shows that the doctrine of legitimate expectations arising from [informal administrative representations] is easy to invoke but difficult to win cases with’).

<sup>64</sup> See, e.g., *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011, para. 227 (‘There is not always a clear distinction between indirect expropriation and violation of legitimate expectations [...]. According to this Tribunal, the violation of a legitimate expectation should rather be protected by the fair and equitable treatment standard’, emphasis omitted).

<sup>65</sup> *International Thunderbird Gaming Corporation v. Mexico*, NAFTA/UNCITRAL, Award, 26 January 2006, Separate Opinion Thomas Wälde, para. 37. See also Katia Yannaca-Small, *Fair and Equitable Treatment Standard*, in *ARBITRATION UNDER INTERNATIONAL INVESTMENT AGREEMENTS* 385, 399 (Katia Yannaca-Small ed., 2010) (noting that ‘obligations entailed in the expropriation clause and those of fair and equitable treatment do not necessarily differ in quality but just in intensity’).



that were taken into account by the foreign investor to make the investment'.<sup>66</sup> The tribunal went on to say that:

The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations. [...] The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities.<sup>67</sup>

This paragraph of the *Tecmed* award has been said to provide 'the most far-reaching exposition of the principle underlying the developing notion of legitimate expectations as applied to fair and equitable treatment in investment law',<sup>68</sup> and has encountered criticism.<sup>69</sup> The *MTD v. Chile* Annulment Committee

<sup>66</sup> *Técnicas Medioambientales Tecmed, S.A. v. Mexico*, ICSID Case No. ARB(AF)/00/2, Award, 29 May 2003, para. 154. Prior to *Tecmed*, a few other tribunals had already hinted at the concept of expectations, however without clearly taking a position as to whether fair and equitable treatment encompasses protection of legitimate expectations. In *Metalclad Corp. v. Mexico*, ICSID Case No. ARB(AF)/97/1, Award, 30 August 2000, the tribunal referred to expectations with a remark of general value in relation to expropriation (para. 103). It only referred to expectations in passing when discussing fair and equitable treatment (see paras. 89, 99, on which see *infra* IV.2.B). It found that the claimant was entitled to rely on the representations of federal officials, and that it had 'the full expectation that the permit would be granted' (*id.*, para. 89). In *ADF Group v. USA*, ICSID Case No. ARB(AF)/00/1, Award, 9 January 2003, para. 189, the tribunal briefly discussed claimant's argument that U.S. case law had created legitimate expectations in the investor, and found that this was not the case, because such expectations had not been created by 'any misleading representations made by authorized officials of the U.S. Federal Government'. Thus, in both *Metalclad* and *ADF* the tribunals seem to proceed on the tacit assumption that a claimant is entitled to rely on the legitimate expectation doctrine under the fair and equitable treatment standard. In *CME Czech Republic B.V. v. The Czech Republic*, UNCITRAL, Partial Award, 13 September 2001, legitimate expectations were mentioned when discussing the parties arguments (see para. 356, setting out Respondent's view), but are not explicitly referred to in the arbitral tribunal's reasoning.

<sup>67</sup> *Técnicas Medioambientales Tecmed, S.A. v. Mexico*, ICSID Case No. ARB(AF)/00/2, Award, 29 May 2003, para. 154, citing to *Neer v. Mexico* case, (1926) R.I.A.A. iv. 60 and International Court of Justice Case: *Eletronica Sicula S.p.A. (ELSI) (United States of America v. Italy)*, 128, p. 65, July 20, 1989, ICJ, General List No. 76.

<sup>68</sup> CAMPBELL MCLACHLAN, LAURENCE SHORE & MATTHEW WEINIGER, INTERNATIONAL INVESTMENT ARBITRATION. SUBSTANTIVE PRINCIPLES 325 (2007). See also *Bayindir Insaat Turizm Ticaret Ve Sanayi A.Ş. v. Pakistan*, ICSID Case No. ARB/03/29, Award, 27 August 2009, para. 179 ('the *Tecmed* case lays out a broad conception of the FET standard').

<sup>69</sup> Zachary Douglas, *Nothing if Not Critical for Investment Treaty Arbitration: Occidental, Eureko and Methanex*, 27(1) ARB. INT'L 27, 28 (2006) (noting that '[t]he *Tecmed* 'standard' is actually not a standard at all; it is rather a description of perfect public regulation in a perfect world, to which all states should aspire but very few (if any) will ever attain. But in the aftermath of the tribunal's correct finding of liability in *Tecmed*, the quoted *obiter dictum* in that award, unsupported by any authority, is now frequently cited by tribunals as the *only* and therefore *definitive* authority for the requirements of fair and equitable treatment'). In *White Industries Australia Limited v. India*, UNCITRAL, Final Award, 30 November 2011, para. 10.3.5, the tribunal referred to the *Tecmed* statement as having been 'subject to what it considers to be

noted that ‘the *TECMED* Tribunal’s apparent reliance on the foreign investor’s expectations as the source of the host State’s obligations (such as the obligation to compensate for expropriation) is questionable.’<sup>70</sup>

A few years after *Tecmed*, the award in *Thunderbird v. Mexico* provided a definition of the concept of legitimate expectation, which has also enjoyed fortune amongst subsequent tribunals. Citing to the principle of good faith and to ‘recent investment case law’, the tribunal observed that:

the concept of “legitimate expectations” relates, within the context of the NAFTA framework, to a situation where a Contracting Party’s conduct creates reasonable and justifiable expectations on the part of an investor (or investment) to act in reliance on said conduct, such that a failure by the NAFTA Party to honour those expectations could cause the investor (or investment) to suffer damages.<sup>71</sup>

Under subsequent jurisprudence, protection of legitimate expectations rapidly became to be considered as the ‘dominant element’<sup>72</sup> or as ‘one of the major components’<sup>73</sup> of the fair and equitable treatment standard.<sup>74</sup> There is in fact no single tribunal on record that has steadfastly refused to find that – at least in principle – such standard encompasses legitimate expectations. Yet, arbitral tribunals have gradually posed limits and qualifications to such recognition. The subsequent analysis will review the contours of the principle as is currently understood in the evolving jurisprudence. In particular, different types of state conduct have been found to arouse legitimate expectations. The following paragraphs attempt to categorize different patterns in relation to which a breach of legitimate expectations has been found by investment treaty tribunals. A distinction between these different types of situations is important because each of them arguably justifies different degrees of legal protection and requires distinct issues to be addressed.

## 2. Distinct situations warranting distinct approaches

### A. Contractual arrangements

In a first series of cases, tribunals have stressed that protection of investors’ legitimate expectations was required under the fair and equitable treatment because the host state had entered into certain contractual commitments with the foreign investors. Contracts are the classical instruments in all legal systems for

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valid criticism’.

<sup>70</sup> MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Chile, ICSID Case No. ARB/01/7, Decision on Annulment, 21 March 2007, paras. 66-78 (internal footnotes omitted). See also CMS Gas Transmission Company v. Argentina, ICSID Case No. ARB/01/08, Decision on Annulment, 25 September 2007, para. 89.

<sup>71</sup> International Thunderbird Gaming Corporation v. Mexico, NAFTA/UNCITRAL, Award, 26 January 2006, paras. 147-48.

<sup>72</sup> Saluka Investments BV v. The Czech Republic, UNCITRAL-PCA, Partial Award, 17 March 2006, para. 302.

<sup>73</sup> EDF (Services) Limited v. Romania, ICSID Case No. ARB/05/13, Award, 8 October 2009, para. 216.

<sup>74</sup> See also *Generation Ukraine, Inc. v. Ukraine*, ICSID Case No. ARB/00/9, Award, 16 September 2003, para. 20.37 (protection of legitimate expectations is ‘a major concern of the minimum standards of treatment contained in bilateral investment treaties’).

the creation of legal stability and predictability,<sup>75</sup> and the expectations that they engender clearly deserve a high level of protection.<sup>76</sup>

When the tribunal in *Continental* attempted to categorise the different types of ‘factors’ upon which the claimant was attempting to base its expectations, it placed expectations arising out of contracts upon the higher stand of protection. The tribunal held that ‘unilateral modification of contractual undertakings by governments [...] deserve clearly more scrutiny [if compared to political statements and general legislative assurances], in the light of the context, reasons, effects, since they generate as a rule *legal rights and therefore expectations of compliance*’.<sup>77</sup>

To give one example of a successful invocation of legitimate expectations arising out of an investment contract one can look at the *MTD v. Chile*.<sup>78</sup> In that case, the investor was able to secure an investment contract with Chile’s foreign investment agency concerning an urban development project. The investor contended that the investment contract, along with other factors, had given rise to the expectation that the project could be carried out successfully (even if the planning regulations would not allow it). The necessary permits were then denied by the Chilean authorities based on the laws in force. The tribunal found that the host state, by entering into the investment contract on the one hand, and by denying the relevant permits on the other, had frustrated the investor’s legitimate expectations and had thus acted unfairly and inequitably.<sup>79</sup>

When considering expectations arising under contracts within the context of a fair and equitable treatment claim, a *caveat* is necessary: even if the investor has an expectation that the contract be fulfilled, a disappointment of such expectation cannot *per se* be equated to a violation of the fair and equitable treaty standard included in the treaty. To reason otherwise would mean that invocation of legitimate expectations would turn the fair and equitable treatment standard into a general umbrella clause, which can hardly be a tenable interpretation.<sup>80</sup>

<sup>75</sup> RUDOLF DOLZER & CHRISTOPH SCHREUER, *PRINCIPLES OF INTERNATIONAL INVESTMENT LAW* 140 (2008).

<sup>76</sup> It should be noted that contracts may also contain stabilization clauses, which provide an additional tool for the investor’s position and may reinforce its expectations. The present section reviews the issues connected with possible expectations arising out of contracts containing no stabilization clauses whereas the specific consequences of such clauses on the investor’s expectations are addressed in the context of the analysis of stability of the legal framework (see *infra* at IV.2.C.a).

<sup>77</sup> *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9, Award, 5 September 2008, para. 261.

<sup>78</sup> *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Chile*, ICSID Case. No. ARB/01/7, Award, 25 May 2004.

<sup>79</sup> *Id.*, paras. 160-167. See ANDREW NEWCOMBE & LLUÍS PARADELL, *LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT* 284-285 (2009).

<sup>80</sup> See Christoph Schreuer, *Fair and Equitable Treatment (FET): interactions with other standards*, in *INVESTMENT PROTECTION AND THE ENERGY CHARTER TREATY* 63, 89-90 (Graham Coop & Clarisse Ribeiro eds., 2008). But see José E. Alvarez, *The Public International Law Regime Governing International Investment*, 344 *RECUEIL DES COURS* 345, fn. 431 (2011) (noting that ‘the emphasis in many FET cases on the need to respect the investors’ “legitimate expectations”, particularly when these are based on specific promises made by the State to the investor, may suggest that even BITs which do not have an “umbrella clause” protecting the investors’ contracts may provide investors with some protection from breaches of their contracts under an FET clause or even under a residual provision protecting the investor “under international law”’).

Case law on this point is rather consistent in distinguishing between legitimate expectations protected under the treaty and purely contractual expectations. In *Parkerings v. Lithuania*, the city of Vilnius had entered into a contract with the investor concerning the construction of a parking system in order to control the traffic in the city's historic old town. The tribunal made the following observation on the issue of contractual expectations:

It is evident that not every hope amounts to an expectation under international law. The expectation a party to an agreement may have of the regular fulfilment of the obligation by the other party is not necessarily an expectation protected by international law. In other words, contracts involve intrinsic expectations from each party that do not amount to expectations as understood in international law. Indeed, the party whose *contractual expectations* are frustrated should, under specific conditions, seek redress before a national tribunal.<sup>81</sup>

Similarly, in *Duke v. Ecuador*, the tribunal noted that 'Electroquil's expectations under the [power purchase agreement] must be regarded as "mere" contractual expectations which are not protected under the BIT'.<sup>82</sup> Also the tribunal in *Hamester v. Ghana* emphasised 'that the existence of legitimate expectations and the existence of contractual rights are two separate issues'.<sup>83</sup> Citing to *Parkerings* with approval, the tribunal concluded that 'the alleged contract violations could not have amounted to a violation of the FET standard based on a theory of "legitimate expectations."<sup>84</sup> *Impregilo v. Argentina* stands for the same proposition.<sup>85</sup>

This line of cases suggests that frustration of contractual expectations is not, *without something further*, susceptible of protection under the fair and equitable standard. This proposition is in harmony with general international law on state responsibility whereby a breach of contract with an alien is not *as such* considered to be a breach of international law.<sup>86</sup> However, case law under investment treaties is not uniform in explaining what this additional element should be. It would seem that for a treaty violation to occur, one would require either 'a breach involving sovereign power' (*puissance publique*),<sup>87</sup> or 'outright and unjustified repudiation

<sup>81</sup> *Parkerings-Compagniet AS v. Lithuania*, ICSID Case No. ARB/05/8, Award, 11 September 2007, para. 344 (emphasis in the original).

<sup>82</sup> *Duke Energy Electroquil Partners and Electroquil SA v. Ecuador*, ICSID Case No. ARB/04/19, Award, 12 August 2008, para. 358.

<sup>83</sup> *Gustav F W Hamester GmbH & Co KG v. Ghana*, ICSID Case No. ARB/07/24, Award, 18 June 2008, para. 335.

<sup>84</sup> *Id.*

<sup>85</sup> *Impregilo S.p.A. v. Argentina*, ICSID Case No. ARB/07/17, Final award, 21 June 2011, para. 292.

<sup>86</sup> See Draft Articles on Responsibility of States for Internationally Wrongful Acts, with commentaries, Art. 4, cmt. para. 6, 53rd Sess. [2001] 2:2 Y.B. INT'L L. COMM'N 40, U.N. Doc. A/56/10 ('Of course the breach by a State of a contract does not as such entail a breach of international law'); F.V. García-Amador, Special Rapporteur, International Responsibility: Fourth Report, [1959] 2 Y.B. INT'L L. COMM'N 30, para. 123, U.N. Doc. A/CN.4/119 (Feb. 26, 1959) ('Diplomatic practice and international caselaw have traditionally accepted almost as dogma the idea that the mere non-performance by a State of its obligations under a contract with an alien individual does not in itself necessarily give rise to international responsibility').

<sup>87</sup> See, e.g., *Consortium R.F.C.C. v. Kingdom of Morocco*, ICSID Case No. ARB/00/6, Award, 22 December 2003, para. 51; *Impregilo S.p.A. v. Pakistan*, ICSID Case No. ARB/03/3, Decision

of the transaction’,<sup>88</sup> or a ‘substantial breach’ ‘under certain limited circumstances’.<sup>89</sup> In the NAFTA case of *Glamis Gold v. USA*, the tribunal agreed with respondent’s view that

a mere contract breach, without something further such as denial of justice or discrimination, normally will not suffice to establish a breach of Article 1105 [minimum standard or treatment]. Merely not living up to expectations cannot be sufficient to find a breach of Article 1105 of the NAFTA.<sup>90</sup>

Thus, the concept of legitimate expectations in these kinds of situations can be accepted as a useful tool to measure the parties’ assumptions when they entered into contractual arrangements, provided, however, the unfair or inequitable treatment by the host state is established by reference to additional factors (beyond the mere non-fulfilment of contract). It is clear that some of the formulations seen above lack the requisite rigor to clearly indicate what such additional element should be when one seeks to understand whether a contract breach qualifies as a treaty breach. This is an area which demands further refinement and where arbitral tribunals will have to provide more precise guidance in the future.<sup>91</sup>

A final point should be made concerning expectations arising out of contracts. It has been seen that contracts engender expectations which have to be placed at the highest stand of protection – contracts usually reflect the carefully negotiated balance achieved by the opposing parties and could be said to crystallize the parties’ expectations. Thus, it will be natural to look at the carefully negotiated contractual terms first to infer what the parties could legitimately expect from the transaction, before turning to more external considerations (such as less formal unilateral representations or the general regulatory context). As noted by Prof. James Crawford, “[r]eference to a general and vague standard of legitimate expectations is no substitute for contractual rights. The relevance of legitimate

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on Jurisdiction, 22 April 2005, para. 260 (referring to Stephen M. Schwebel, *On Whether the Breach by a State of a Contract with an Alien is a Breach of International Law*, in JUSTICE IN INTERNATIONAL LAW: SELECTED WRITINGS 425 (Stephen M. Schwebel ed., 1994)); *Duke Energy Electroquil Partners and Electroquil SA v. Ecuador*, ICSID Case No. ARB/04/19, Award, 12 August 2008, paras. 342-343; *Toto Construzioni Generali S.p.A. v. Lebanon*, ICSID Case No. ARB/07/12, Award, 7 June 2012, paras. 161-162. But see RUDOLF DOLZER & CHRISTOPH SCHREUER, *PRINCIPLES OF INTERNATIONAL INVESTMENT LAW* 142 (2008).

<sup>88</sup> *Waste Management, Inc. v. Mexico*, ICSID Case No. ARB(AF)/00/3, Award, 30 April 2004, para. 115.

<sup>89</sup> *Parkerings-Compagniet AS v. Lithuania*, ICSID Case No. ARB/05/8, Award, 11 September 2007, para. 316.

<sup>90</sup> *Glamis Gold, Ltd. v. USA*, NAFTA/UNCITRAL, Award, 8 June 2009, para. 620 (citing to *Azinian v. United Mexican States*, ICSID Case No. ARB/(AF)/97/2, Award, 1 November 1999, para. 87).

<sup>91</sup> See also Christoph Schreuer, *Fair and Equitable Treatment in Arbitral Practice*, 6(3) *JOURNAL OF WORLD INVESTMENT & TRADE* 357, 380 (2005) (suggesting that ‘a wilful refusal by a government authority to abide by its contractual obligations, abuse of government authority to evade agreements with foreign investors and action in bad faith in the course of contractual performance may well lead to a finding that the standard of fair and equitable treatment has been breached’).



expectations is not a licence to arbitral tribunals to rewrite the freely negotiated terms of investment contracts”.<sup>92</sup>

### B. Informal representations

Claimants in investment treaty arbitrations have often invoked the concept of legitimate expectations when the host state allegedly made certain promises or representations, on which the investor relied at the time of making its investment and the disappointment of which caused the investor to suffer damages. Sometimes the cases may not be easily categorised, because the factual pattern may involve both a contract and some kind of informal representations, which is invoked usually to reinforce those contractual commitments. Alternatively, representations are invoked in addition to alleged guarantees to be found in the regulatory framework (on which see *infra* IV.2.C). Yet, in other cases we are in presence merely of unilateral representations. It is thus important to examine whether and to what extent a promise, assurance, or comfort letter is capable of arousing legitimate expectations, frustrations of which would entail a violation of fair and equitable treatment. Investment treaty tribunals have been willing to extend protection based on the theory of legitimate expectations in a number of cases.

As early as in *SPP v. Egypt*, where the jurisdiction of the ICSID arbitral tribunal did not arise under an investment treaty but under Egypt’s domestic law, did the tribunal recognize that the investor was entitled to rely, as a matter of international law, on certain decisions by certain high-ranking Government officials:

82. It is possible that under Egyptian law certain acts of Egyptian officials including even Presidential Decree No. 475 may be considered legally nonexistent or null and void or susceptible to invalidation. However, these acts were cloaked with the mantle of Government authority and communicated as such to foreign investors who relied on them in making their investments.

83. Whether legal under Egyptian law or not, the acts in question were the acts of Egyptian authorities, including the highest executive authority of the Government. These acts, which are now alleged to have been in violation of the Egyptian municipal legal system, *created expectations protected by established principles of international law*.<sup>93</sup>

This case, according to Dolzer and Schreuer, would suggest that there is authority to the effect that ‘the investor’s legitimate expectations are protected even without a treaty guarantee of FET’.<sup>94</sup>

Within the investment treaty context, jurisprudence on this issue is quite rich, and one can find several statements to the effect that an investor is able to rely on the host state’s representations.

<sup>92</sup> James Crawford, *Treaty and Contract in Investment Arbitration*, 24(3) ARB. INT’L 351, 373 (2008).

<sup>93</sup> Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt, ICSID Case No. ARB/84/3, Award and Dissenting Opinion, 20 May 1992, paras. 82-83 (emphasis added).

<sup>94</sup> RUDOLF DOLZER & CHRISTOPH SCHREUER, *PRINCIPLES OF INTERNATIONAL INVESTMENT LAW* 135 (2008).

One oft-cited passage is the statement made by the *Waste Management*:

In applying [the fair and equitable treatment] standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.<sup>95</sup>

In *Sempra v. Argentina* the tribunal, after recalling the *Tecmed* standard, noted that:

[The requirement to protect legitimate expectations] becomes particularly meaningful when the investment has been attracted and induced by means of assurances and representations...<sup>96</sup>

This teleological element (that is, representations must have had the purpose of *inducing* the investment) was also stressed by the tribunal in *Glamis Gold v. USA*:

a State may be tied to the objective expectations that it creates *in order to induce* investment. Such an upset of expectations thus requires something greater than mere disappointment; it requires, as a threshold condition, the active inducement of a quasi-contractual expectation.<sup>97</sup>

The tribunal in the already cited *Parkerings v. Lithuania* case further observed that:

[An] expectation is legitimate if the investor received an explicit promise or guaranty from the host-State, or if implicitly, the host-State made assurances or representation that the investor took into account in making the investment. Finally, in the situation where the host-State made no assurance or representation, the circumstances surrounding the conclusion of the agreement are decisive to determine if the expectation of the investor was legitimate.<sup>98</sup>

The final part of the *Parkerings* passage flags the issue of whether an expectation may arise irrespective of the presence of a representation or assurance. The tribunal does not seem to rule out this possibility, depending on the surrounding circumstances.<sup>99</sup> Again, one must bear in mind that there was in this case a contract between the city and the investor.

<sup>95</sup> *Waste Management, Inc. v. Mexico*, ICSID Case No. ARB(AF)/00/3, Award, 30 April 2004, para. 98. This passage was cited with approval by many subsequent tribunals, amongst which see, e.g., *EDF (Services) Limited v. Romania*, ICSID Case No. ARB/05/13, Award, 8 October 2009, para. 216 (noting that '[protection of legitimate expectations] comes into consideration whenever the treatment attributable to the State is in breach of representations made by it which were said to be reasonably relied upon by the Claimant').

<sup>96</sup> *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Award, 28 September, para. 298.

<sup>97</sup> *Glamis Gold, Ltd. v. USA*, NAFTA/UNCITRAL, Award, 8 June 2009, para. 766.

<sup>98</sup> *Parkerings-Compagniet AS v. Lithuania*, ICSID Case No. ARB/05/8, Award, 11 September 2007, para. 331.

<sup>99</sup> See also *Saluka Investments BV v. The Czech Republic*, UNCITRAL-PCA, Partial Award, 17 March 2006, para. 329 ('The Tribunal finds that the Claimant's reasonable expectations to be

*Thunderbird v. Mexico* presents a clear case where the investor could neither invoke contractual commitments with the host state, nor any unilaterally granted administrative acts (permits or licenses). Thunderbird thus essentially relied on a legal opinion (the '*Oficio*') given to it by the Mexican authorities concerning the legality of its proposed gaming operations. After the investment was made, the Mexican authorities shut down the relevant facilities because they were found to involve a considerable degree of chance, in violation of the gambling prohibition in the host state. The tribunal discussed the issue of legitimate expectations and found, by majority, that the *Oficio* could not generate a legitimate expectations upon which the investor could reasonably rely in operating its gaming machines in Mexico.<sup>100</sup> It proved fatal to the case the fact that the investor, in seeking such legal opinion, had not disclosed relevant information as to the nature of the gaming machines, thereby 'put[ting] the reader on the wrong track'.<sup>101</sup>

In sum, arbitral practice thus confirms that representations by the host state are, in principle, capable of generating legitimate expectations, and may be protected under the fair and equitable treatment, if they are later repudiated by the state. This position is in line with what happens in the domestic administrative systems, which, as seen, treat those instances as particularly worthy of protection.

*Specificity of the representation.* It is also clear from investment case law that not each and every representation or assurance is amenable to arouse legitimate expectations. It has been seen above that domestic legal systems as well as EU law require a certain grade of precision or lack of ambiguity for representations to be enforced under the theory of legitimate expectations. Investment treaty jurisprudence is likewise consistent in requiring a certain level of specificity. The requirement that a promise be specific may, in a first meaning, concern the object (i.e., the content) and the unambiguous form of the representation. In a different sense, specificity means individualisation, i.e., the promise or representation is addressed to the individual investor, and not to the generality.<sup>102</sup> Such latter distinction assumes particular importance when expectations are grounded in instruments of general application (such as legislation), and will be also addressed later when dealing with the issue of stability.

In *Frontier Petroleum v. Czech Republic*, the tribunal reviewed two letters sent by the Czech Ministry of Industry and Trade to claimant, in which the Ministry indicated that 'the state would have the possibility to enter into negotiations' with the investor.<sup>103</sup> The tribunal found this not be an 'undertaking',

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entitled to protection under the Treaty need not be based on an explicit assurance from the Czech Government'); Grand River Enterprises Six Nations Ltd et al. v. USA, NAFTA/UNCITRAL, Award, 12 January 2011, paras. 140-141 (holding that '[t]he Tribunal understands the concept of reasonable or legitimate expectations in the NAFTA context to correspond with those expectations upon which an investor is entitled to rely as a result of representations or conduct by a state party [...] Ordinarily, reasonable or legitimate expectations of the kind protected by NAFTA are those that arise through targeted representations or assurances made explicitly or implicitly by a state party').

<sup>100</sup> International Thunderbird Gaming Corporation v. Mexico, NAFTA/UNCITRAL, Award, 26 January 2006, paras. 145-166.

<sup>101</sup> *Id.*, para. 155.

<sup>102</sup> For this distinction, see also *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011, paras. 375-377.

<sup>103</sup> *Frontier Petroleum Services Ltd v. Czech Republic*, UNCITRAL/PCA, Final Award, 12 November 2010, paras. 76, 455.

but merely a ‘signal to Claimant that there was a possibility that the state could negotiate’.<sup>104</sup> The two letters ‘did not provide an adequate basis for the Claimant to rely on some form of representation or expectation’, and they did ‘not exhibit the level of specificity necessary to generate legitimate expectations.’<sup>105</sup>

In *White Industries v. India*, the claimant argued that Indian officials had made representations to one of the claimant’s directors when he was travelling to India with a view to establishing his investment. Allegedly such representations were to the effect that ‘it was safe for Claimant to invest in India and that the Indian legal system was, to all intents and purposes, the same as the Australian legal system.’<sup>106</sup> The Tribunal found that those representations did not meet the requisite level of specificity for the purpose of arousing legitimate expectations amenable to be protected under the fair and equitable treatment standard.<sup>107</sup>

*Metalclad v. Mexico* concerned a dispute arising from the construction of a hazardous waste landfill. The investor had secured the necessary permits at both the federal and state level. It lacked a permit on the municipal level, but received repeated assurances by federal officials that such permit was not needed, and that the municipality would have no legal basis for denying the permit. After several failed attempts to reach a solution to the *impasse*, Metalclad filed a NAFTA Chapter 11 claim. The tribunal found that fair and equitable treatment had been breached because, *inter alia*, the municipality’s denial of the permit was improper and Metalclad could rely upon the representations of the Federal Government. The tribunal held that:

Metalclad was entitled to rely on the representations of federal officials and to believe that it was entitled to continue its construction of the landfill. In following the advice of these officials, and filing the municipal permit application [...], Metalclad was merely acting prudently and in the full expectation that the permit would be granted.<sup>108</sup>

In *Feldman v. Mexico*, the tribunal contrasted the assurances at issue in the case with those given by the Mexican authorities in *Metalclad* (which the *Feldman* tribunal referred to as ‘definitive, unambiguous and repeated’),<sup>109</sup> and found that those given to Feldman were ‘at best ambiguous and largely informal’.<sup>110</sup> Also Wälde in his Separate Opinion in *Thunderbird*, though adopting a broad notion of protection of legitimate expectations, concedes that ‘a legitimate expectation is assumed more readily if an individual investor receives specifically formal assurances that display visibly an official character’.<sup>111</sup> The threshold is thus ‘quite high’.<sup>112</sup>

<sup>104</sup> Id., para. 465.

<sup>105</sup> Id., para. 468.

<sup>106</sup> *White Industries Australia Limited v. India*, UNCITRAL, Final Award, 30 November 2011, para. 5.2.6.

<sup>107</sup> Id., para. 10.3.17 (holding that ‘the alleged representations suffer from vagueness and generality, such that they are not capable of giving rise to reasonable legitimate expectations that are amenable to protection under the fair and equitable treatment standard’).

<sup>108</sup> *Metalclad Corp. v. Mexico*, ICSID Case No. ARB(AF)/97/1, Award, 30 August 2000, para. 89.

<sup>109</sup> *Feldman v. Mexico*, ICSID Case No. ARB(AF)/99/1, Award, 16 December 2002, para. 148.

<sup>110</sup> Id., para. 149.

<sup>111</sup> *International Thunderbird Gaming Corporation v. Mexico*, NAFTA/UNCITRAL, Award, 26 January 2006, Separate Opinion Thomas Wälde, para. 32.

<sup>112</sup> Id.

Statements of a more general nature issued by politicians in varying contexts or general investment-encouraging policies directed towards investors have also been sometimes invoked as a basis of legitimate expectations. Arbitral tribunals have treated them differently. In *BG v. Argentina*, the fair and equitable treatment claim was mostly based on the breach of guarantees contained in the regulatory framework. However, the tribunal mentioned the message to Congress by Argentina's president when requesting the ratification of the relevant bilateral investment treaty,<sup>113</sup> and a so-called 'information memorandum' prepared by Argentina to promote the privatization of a state-owned gas company,<sup>114</sup> as additional elements on which the investor could rely when making its investment.<sup>115</sup> The concrete effect of these declarations or documents on legitimate expectations and on the breach of the fair and equitable treatment are however difficult to assess, given that what was decisive for the tribunal's finding was the breach of the 'guarantees' contained in the regulatory framework.<sup>116</sup>

The *MTD v. Chile* award mentions repeatedly the Chilean President's toast speech at a dinner with the President of Malaysia (the home state of the investor) praising the real estate project at issue, as well as his public statement sent to be read at the inauguration of the project.<sup>117</sup> The tribunal would seem to have taken those acts into account when evaluating the investor's expectations.<sup>118</sup>

In *PSEG v. Turkey*, the host state's policy to encourage and welcome investment could not found a claim of legitimate expectations. After noting that '[l]egitimate expectations by definition require a promise of the administration on which the Claimants rely to assert a right that needs to be observed',<sup>119</sup> the tribunal held that the general investment encouragement policy pursued by Turkey 'did not entail a promise made specifically to the Claimants about the success of their proposed project'.<sup>120</sup>

In *Continental v. Argentina*, the claimant relied on 'Argentina's representations to keep its money in Argentina',<sup>121</sup> as well as on 'certain public statements by Minister Cavallo, undertaking not to abandon the convertibility

<sup>113</sup> *BG Group Plc. v. Argentina*, UNCITRAL, Final Award, 24 December 2007, para. 300.

<sup>114</sup> *Id.*, paras. 171, 172, 305.

<sup>115</sup> *Id.*, paras. 306-310.

<sup>116</sup> Similarly see *LG&E Energy Corp et al. v. Argentina*, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006, paras. 50 and 175. Also in *Sempra Energy International v. Argentina*, ICSID Case No. ARB/02/16, Award, 28 September 2007, did the investor invoke the 'offering memorandum', that it had been given before the bidding process, and which explained the guarantees contained in regulatory framework (paras. 84, 105, 110). Argentina disputed the significance of such memorandum, in view of the fact that it had been prepared by private consultants, that the Government had expressly disclaimed responsibility, and that it contained errors (*id.*, para. 113). The tribunal found it unlikely that 'such errors would have passed unnoticed by competent government officials. Moreover, the Government would in such a situation have been duty-bound to issue a clarification to avoid the engendering of a false legitimate expectation. No such clarification was ever issued' (*id.*). The Tribunal thus sided with the claimant and appeared to find in the memorandum an additional basis for protecting the investor's expectations. See also *id.*, para. 141.

<sup>117</sup> *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Chile*, ICSID Case. No. ARB/01/7, Award, 25 May 2004, paras. 63, 125, 133, 156-157.

<sup>118</sup> *Id.*, para. 158.

<sup>119</sup> *PSEG v. Turkey*, ICSID Case No. ARB/02/5, Award, 19 January 2007, para. 241.

<sup>120</sup> *Id.*, para. 243.

<sup>121</sup> *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9, Award, 5 September 2008, para. 252



regime'.<sup>122</sup> The tribunal refused to find that legitimate expectations had been frustrated by way of repudiation of such statements and held that

in order to evaluate the relevance of [the “reasonable legitimate expectations” concept] applied within Fair and Equitable Treatment standard and whether a breach has occurred, relevant factors include:

i) the specificity of the undertaking allegedly relied upon which is mostly absent here, considering moreover that political statements have the least legal value, regrettably but notoriously so.<sup>123</sup>

Also in *El Paso*, claimant relied on a general message to the Congress by the Argentine President jointly with Minister Cavallo about the ‘legal certainty’ that the enactment of the Electricity Law would achieve.<sup>124</sup> The tribunal observed that ‘a declaration made by the President of the Republic clearly must be viewed by everyone as a political statement, and this Tribunal is aware, as is every individual, of the limited confidence that can be given to such political statements in all countries of the world’.<sup>125</sup> Although the Tribunal conceded that such statements may have induced investors to decide to invest in Argentina, they did not equate to a ‘a specific commitment to foreign investors not to modify the existing framework, which was designed to attract them’.<sup>126</sup>

The claimant had also relied on the fact that ‘in order to promote investments in the Electricity Sector and to explain the Regulatory Framework, the Government had organised road shows, conferences and seminars to explain the main features of the Framework and to give assurance to investors that their rights would be protected’.<sup>127</sup> In the Claimant’s opinion such conduct should be equated to ‘unilateral declarations’ akin to those that were considered binding by the ICJ in the *Nuclear Tests* cases. The tribunal refused to follow the analogy, holding that ‘no lesson can be drawn from the *Nuclear Tests* cases to give legal weight to investment-promoting road shows’, and that ‘such political and commercial incitements cannot be equated with commitments capable of creating reasonable expectations protected by the international mechanism of the BIT’.<sup>128</sup>

This last passage from the *El Paso* award raises the question as to whether the rules on unilateral acts which have developed on the inter-state level may be applicable by analogy in an investor-state context. This could be a different way of conceptualizing the binding effect on states of their promises towards investors. Prof. Michael Reisman and Dr. Mahnoush Arsanjani have explored this question in a seminal article, and have concluded that:

Where a host State which seeks foreign investment acts intentionally, so as to create expectations in potential investors with respect to particular treatment or comportment, the host State should [...] be bound by the

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<sup>122</sup> Id.

<sup>123</sup> Id., para. 261 (internal footnote omitted).

<sup>124</sup> Id., para. 393.

<sup>125</sup> Id., para. 395.

<sup>126</sup> Id., paras. 395-396.

<sup>127</sup> *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011, para. 392.

<sup>128</sup> Id.

commitments and the investor is entitled to rely upon them in instances of decision.<sup>129</sup>

It may in fact be argued that the binding nature of a unilateral act on an inter-state level is at least partly connected with the expectation that such act creates in third states. This seems to have been expressly recognized by the ICJ in *Nuclear Tests*, in which the Court linked the binding character of unilateral declaration to the principle of good faith, mentioning also the protection of trust and confidence which third states may place on such declarations.<sup>130</sup> When the topic of unilateral acts was dealt with by the International Law Commission (ILC), the debate turned several times on the ultimate foundation for the binding nature of unilateral acts. Along with the opinion that such binding character rested on the intent or will of the state making the declaration, a different opinion precisely pointed to the *expectation* that the declaration creates in other states.<sup>131</sup> The final text of the Guiding Principles on unilateral declaration of states, approved in 2006 by the ILC, records, in its preamble, that ‘in practice, it is often difficult to establish

<sup>129</sup> W. Michael Reisman & Mahnoush H. Arsanjani, *The Question of Unilateral Governmental Statements as Applicable Law in Investment Disputes*, in *VÖLKERRECHT ALS WERTORDNUNG – COMMON VALUES IN INTERNATIONAL LAW*, FESTSCHRIFT FÜR: ESSAYS IN HONOUR OF CHRISTIAN TOMUSCHAT 409, 422 (P.M. Dupuy et al. eds., 2006).

<sup>130</sup> See *Nuclear Tests*, I.C.J. Reports 1974, p. 268, para. 46; p. 473, para. 49 (‘One of the basic principles governing the creation and performance of legal obligations, whatever their source, is the principle of good faith. Trust and confidence are inherent in international co-operation, in particular in an age when this co-operation in many fields is becoming increasingly essential. Just as the very rule of *pacta sunt servanda* in the law of treaties is based on good faith, so also is the binding character of an international obligation assumed by unilateral declaration. Thus interested States may take cognizance of unilateral declarations and place confidence in them, and are entitled to require that the obligation thus created be respected’). See in particular Robert Kolbe, *Principles as Sources of International Law (With Special Reference to Good Faith)*, 53 *NETHERLANDS INTERNATIONAL LAW REVIEW* 1, 10 (2006) (noting that ‘when in 1974 the International Court was faced with the necessity to argue the binding nature of unilateral declarations, it found support in that idea of legitimate expectations, since it had recourse to the principle of good faith in its famous paragraph 46 at page 268’).

<sup>131</sup> See International Law Commission, *First Report on Unilateral Acts of States*, 5 March 1998, U.N. Doc. A/CN.4/486, paras. 160-162 (‘The State which formulates the declaration is bound to fulfil the obligation which it assumes, not because of the potential juridical interest of the addressee but because of the intention of the State making the declaration. [...] Necessary confidence in the relationships and expectations which are created by a State which formulates a declaration and assumes an engagement also found or justify the binding nature of that declaration’); *Report of the International Law Commission on the work of its fifty-second session (2000). Topical summary of the discussion held in the Sixth Committee of the General Assembly during its fifty-fifth session prepared by the Secretariat*, 15 February 2001, U.N. Doc. A/CN.4/513 (‘according to one view, it was doubtful whether the intention of the author State, although highly relevant, should be seen as the sole or fundamental criterion in the definition of a unilateral act; a unilateral act was binding not only to the extent that such was the intention of the author State but also inasmuch as it created legitimate expectations’); *Report of the International Law Commission on the Work of its Fifty-fourth Session* (Apr. 29-June 7 and July 22-Aug. 16, 2002), paras. 335-349; Summary Record of the 2593rd Meeting, 24 June 1999, U.N. Doc. A/CN.4/SR.2593, para. 73 (comment by Bruno Simma adhering to the view that ‘unilateral promises or other statements could become binding only if another party expected the promising State to keep its promises. That expectation created a legal obligation’); Summary Record of the 2818th meeting, 16 July 2004, U.N. Doc. A/CN.4/SR.2818, paras. 1-4 (comment by Martti Koskenniemi, reviewing the two possible foundations for the binding nature of unilateral acts, and expressing scepticism as to both approaches).

whether the legal effects stemming from the unilateral behaviour of a State are the consequence of the intent that it has expressed or *depend on the expectations that its conduct has raised* among other subjects of international law'.<sup>132</sup>

Thus, one finds support also in the public international law rules on unilateral acts for the contention that representations made by a state, from which it later resiles, engender expectations that are worthy of protection. These public international rules could be applied by analogy within the investor-state context. Certain investment tribunals have recently accepted this proposition, although in the context of the analysis of a different issue, i.e. the interpretation of consent to arbitration contained in a piece of domestic legislation.<sup>133</sup> The tribunals in those cases recalled ICJ case law on the interpretation of unilateral declarations,<sup>134</sup> and quoted the ILC Guiding Principles.<sup>135</sup> Outside of these examples on consent, arbitral tribunals have generally not invoked international law rules on unilateral acts when dealing with representations or promises of a substantive nature (such as the ones that more closely concern us here). As seen, they have rather preferred to follow the well-trodden path of legitimate expectations. The *El Paso* tribunal, in the above mentioned passage, refused the proposed analogy with the *Nuclear Tests* cases, yet not as a matter of legal principle, it would seem, but because it found the acts at issue to be factually very different. In any event, one must note that, even if one were to apply general international law rules on unilateral declarations, and in particular the ILC 2006 Guiding Principles on this issue, the state's declaration would entail obligations for the formulating state 'only if it is stated in clear and specific terms'.<sup>136</sup> Thus, as can be seen, the standard to hold a state to its representation would not in the end be different to the one that investment tribunals have articulated through the doctrine of legitimate expectations in the consistent line of cases analysed above.

### C. General regulatory framework

In a third type of situation, investors claim that their expectations were grounded in the general legislative and regulatory framework as in force when they made their investment, which the host state later changed so as to frustrate such expectations, in breach of the fair and equitable treatment standard. The

<sup>132</sup> *Guiding Principles applicable to unilateral declarations of States capable of creating legal obligations, with commentaries thereto*, in ILC Report on the Work of its Fifty-Eighth Session (May 1-June 9 and July 3-Aug. 11, 2006), U.N. Doc. A/61/10, at 369 (emphasis added).

<sup>133</sup> See *Mobil Corp. et al. v. Venezuela*, ICSID Case No. ARB/07/27, Decision on Jurisdiction, 10 June 2010, paras. 84-96; *CEMEX Caracas Investments BV and CEMEX Caracas II Investments BV v. Venezuela*, ICSID Case No. ARB/08/15, Decision on Jurisdiction, 30 December 2010, paras. 77-89. See Michele Potestà, *The Interpretation of Consent to ICSID Arbitration Contained in Domestic Investment Laws*, 27(2) *ARB. INT'L* 149 (2011).

<sup>134</sup> *Mobil Corp. et al. v. Venezuela*, ICSID Case No. ARB/07/27, Decision on Jurisdiction, 10 June 2010, paras. 88-96; *CEMEX Caracas Investments BV and CEMEX Caracas II Investments BV v. Venezuela*, ICSID Case No. ARB/08/15, Decision on Jurisdiction, 30 December 2010, paras. 82-89, both quoting the *Guiding Principles applicable to unilateral declarations of States capable of creating legal obligations, with commentaries thereto*, in ILC Report on the Work of its Fifty-Eighth Session (May 1-June 9 and July 3-Aug. 11, 2006), U.N. Doc. A/61/10 at 367.

<sup>135</sup> *Mobil Corp. et al. v. Venezuela*, ICSID Case No. ARB/07/27, Decision on Jurisdiction, 10 June 2010, paras. 81-82; *CEMEX Caracas Investments BV and CEMEX Caracas II Investments BV v. Venezuela*, ICSID Case No. ARB/08/15, Decision on Jurisdiction, 30 December 2010, paras. 87, 89.

<sup>136</sup> Principle 7 of the ILC Guiding Principles.

issue that an arbitral tribunal faces in such a case is, in the words of the *Total* tribunal, ‘to determine whether the legislation, regulation and provisions invoked by [claimant] constitute a set of promises and commitments [...] whose unilateral modifications entail a breach of the legitimate expectations [...]’.<sup>137</sup> The difference between the two situations seen above (where there is either a formal arrangement between the parties, or the host state has at least given an informal (but specific) representation) is clear, because in this third scenario ‘investor’s expectations are rooted in regulation of a normative and administrative nature that is not specifically addressed to the relevant investor’.<sup>138</sup>

The starting point which is rather uncontroversial is that the investor must take the local law as it stands at the time of making the investment (which means the investor cannot subsequently complain about the application of *that* law to its investment).<sup>139</sup> It is at that moment in time that the expectations are assessed.<sup>140</sup> But to what extent is the investor legitimately entitled to expect that such law is not going to change *after* it has performed its investment?

When analysing the domestic administrative law protection of legitimate expectations, it has been seen that domestic systems have been cautious to extend protection in these sets of circumstances.<sup>141</sup> When it looked at those domestic law systems to draw parallels with investment treaty law, the *Total* tribunal

<sup>137</sup> *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 99.

<sup>138</sup> *Id.*, para. 122.

<sup>139</sup> For an early application of this principle, see *The Oscar Chinn Case*, PCIJ Series A/B No 63 (1934), pp. 19-23, at 23. See also Rudolf Dolzer, ‘Fair and Equitable Treatment: A Key Standard in Investment Treaties’, 39 *INTERNATIONAL LAWYER* 87, 102-103 (2005); RUDOLF DOLZER & CHRISTOPH SCHREUER, *PRINCIPLES OF INTERNATIONAL INVESTMENT LAW* 134-135 (2008).

<sup>140</sup> See Christoph Schreuer & Ursula Kriebaum, *At What Time Must Legitimate Expectations Exist?*, in *A LIBER AMICORUM: THOMAS WÄLDE. LAW BEYOND CONVENTIONAL THOUGHT* 265-276 (Jacques Werner & Arif H. Ali eds., 2009). For cases holding that expectations must be assessed at the time of making the investment, see *LG&E Energy Corp et al. v. Argentina*, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006, para. 130 (‘[expectations] are based on the conditions offered by the host State at the time of the investment’); *Duke Energy Electroquil Partners and Electroquil SA v. Ecuador*, ICSID Case No. ARB/04/19, Award, 12 August 2008, paras. 340 (‘expectations must be legitimate and reasonable at the time when the investor makes the investment’) and 365 (excluding protection of expectations arising out of two agreements, which were signed two years after the decision to invest); *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9, Award, 5 September 2008, para. 259 (rejecting the existence of legitimate expectations based on general legislative ‘assurances’ because the investor had entered the host state before those assurances were made); *National Grid P.L.C. v. Argentina*, UNCITRAL, Award, 3 November 2008, para. 173; *Bayindir Insaat Turizm Ticaret Ve Sanayi A.Ş. v. Pakistan*, ICSID Case No. ARB/03/29, Award, 27 August 2009, para. 190; *Joseph Charles Lemire*, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability, 14 January 2010, para. 264; *Aes Summit Generation Limited and Aes-Tisza Erömu Kft v. Republic of Hungary*, ICSID Case No. ARB/07/22, Award, 23 September 2010, paras. 9.3.12-9.3.16; *Frontier Petroleum Services Ltd v. Czech Republic*, UNCITRAL/PCA, Final Award, 12 November 2010, paras. 287-288 (noting that ‘when investments are made through several steps, spread over a period of time, legitimate expectations must be examined for each stage at which a decisive step is taken towards the creation, expansion, development, or reorganisation of the investment’) and 468. But see *Kardassopoulos v. Georgia* and joined case, ICSID Case Nos ARB/05/18 and ARB/07/15, Award, 28 February 2010, paras. 439-441.

<sup>141</sup> See *supra* III.

highlighted that ‘only exceptionally has the concept of legitimate expectations been the basis of redress when legislative actions by a state was at stake’.<sup>142</sup>

Yet, the argument that a claimant may be able to rely on expectations purely based on the regulatory framework has enjoyed a certain fortune in the investment treaty context. This approach has usually been justified on the grounds that the fair and equitable treatment standard would entail an element of stability of the regulatory framework. Thus, in a first line of cases, certain tribunals have been willing to extend protection under the fair and equitable treatment so as to cover the state’s duty to maintain a stable framework. This sub-element of the standard has been often buttressed through a reference to the BIT’s preamble, which may refer to stability as one of the goals of the treaty.<sup>143</sup> Thus, the tribunal in *Occidental Exploration & Production Co. (OEPC) v. Ecuador*, for example, referred to the preamble of the BIT to conclude that ‘stability of the legal and business framework is [...] an essential element of fair and equitable treatment’<sup>144</sup> and that ‘there is certainly an obligation not to alter the legal and business environment in which the investment has been made’.<sup>145</sup> Most of the first generation Argentine cases have turned on the issue of stability of the regulatory framework. However, one has to note that in those cases the investors could also invoke licenses (granted by the government by decree), which, in addition to referring to the guarantees established by legislation, also stated that they could not be modified without the licensee’s consent. Those licenses can be considered part of the regulatory framework, yet at the same time they are certainly more individualised than a piece of general legislation. It is thus difficult to evaluate exactly what role the presence of such licenses have played for the tribunals’ finding of breach of the fair and equitable treatment, although certain far-reaching *dicta* would seem to suggest that expectations arising from the regulatory framework would alone have been sufficient for such a finding. In *CMS v. Argentina*, for example, the tribunal drew on the preamble of the applicable BIT to hold that ‘stable legal and business environment is an essential element of fair and equitable treatment’.<sup>146</sup> By entirely altering and transforming the legal business environment under which the investment was decided and made, Argentina had violated the fair and equitable treatment standard.<sup>147</sup> The *LG&E v. Argentina* tribunal cited to the developing jurisprudence on the stability requirement as providing ‘an emerging standard of fair and equitable treatment in

<sup>142</sup> Total S.A. v. Argentina, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 129.

<sup>143</sup> See, in addition to the cases discussed *infra*, Joseph Charles Lemire, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability, 14 January 2010, para. 264 (noting that ‘[w]ords used in treaties must be interpreted through their context. The context of Article II.3 is to be found in the Preamble of the BIT, in which the contracting parties state “that fair and equitable treatment of investment is desirable in order to maintain a stable framework for investment...”’. The FET standard is thus closely tied to the notion of legitimate expectations - actions or omissions by Ukraine are contrary to the FET standard if they frustrate legitimate and reasonable expectations on which the investor relied at the time when he made the investment’ (emphasis omitted, internal footnote omitted)).

<sup>144</sup> Occidental Exploration and Production Company v. Ecuador, UNCITRAL/LCIA Case No. UN 3467, Final Award, 1 July 2004, para. 183.

<sup>145</sup> *Id.*, para. 191.

<sup>146</sup> CMS Gas Transmission Company v. Argentina, ICSID Case No. ARB/01/08, Award, 12 May 2005, para. 274.

<sup>147</sup> *Id.*, paras. 266-284.



international law'.<sup>148</sup> It found that, by violating or taking away the guarantees embodied in the relevant laws and regulations in the gas sector, Argentina 'completely dismantl[ed] the very legal framework constructed to attract investors',<sup>149</sup> and thus violated the fair and equitable treatment standard.<sup>150</sup> In *Enron v. Argentina*, the tribunal held that a 'key element of fair and equitable treatment is the requirement of a "stable framework for the investment"',<sup>151</sup> along with the requirement to protect legitimate expectations.<sup>152</sup> The tribunal added that 'it was in reliance upon the conditions established by the Respondent in the regulatory framework for the gas sector that Enron embarked on its investment' and that 'Enron had reasonable grounds to rely on such conditions'.<sup>153</sup> By 'dismantling' the regulatory framework, Argentina had failed to provide a stable framework as required by the BIT, thereby acting unfairly and inequitably.<sup>154</sup>

In contradistinction, certain tribunals have stressed that as a matter of principle the state's right to regulate cannot be considered frozen or restricted as a result of the existence of investment treaties.

In *Saluka*, one can find repeated statements to the effect that no investor may reasonably expect that the circumstances prevailing at the time the investment is made remain totally unchanged.<sup>155</sup> And in *Parkerings v. Lithuania*, the tribunal required due diligence from the investor, who 'must anticipate that the circumstances could change, and thus structure its investment in order to adapt it to the potential changes of legal environment'.<sup>156</sup>

The three tribunals in the Argentine cases of *Continental*, *Total*, and *El Paso* devoted long discussions to distance themselves from that line of case law recalled above, which combined expectations and stability of the regulatory framework. For example, in *Continental*, the tribunal made the forceful statement that:

it would be unconscionable for a country to promise not to change its legislation as time and needs change, or even more to tie its hands by such a kind of stipulation in case a crisis of any type or origin arose. Such an implication as to stability in the BIT's Preamble would be contrary to an effective interpretation of the Treaty; reliance on such an implication by a foreign investor would be misplaced and, indeed, unreasonable.<sup>157</sup>

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<sup>148</sup> LG&E Energy Corp et al. v. Argentina, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006, para. 125. See also *id.*, para. 131 (where the tribunal found fair and equitable treatment standard to consist in the host state's behaviour that involves 'the obligation to grant and maintain a stable and predictable legal framework necessary to fulfill the justified expectations of the foreign investor').

<sup>149</sup> *Id.*, para. 139.

<sup>150</sup> *Id.*, paras. 132-139.

<sup>151</sup> Enron Corporation Ponderosa Assets, L.P. v. Argentina, ICSID Case No. ARB/01/3, Award, 22 May 2007, para. 260 (emphasis in the original).

<sup>152</sup> *Id.*, para. 262.

<sup>153</sup> *Id.* para. 265.

<sup>154</sup> *Id.*, paras. 251-268.

<sup>155</sup> Saluka Investments BV v. The Czech Republic, UNCITRAL-PCA, Partial Award, 17 March 2006, paras. 305, 351.

<sup>156</sup> Parkerings-Compagniet AS v. Lithuania, ICSID Case No. ARB/05/8, Award, 11 September 2007, para. 333.

<sup>157</sup> Continental Casualty Company v. Argentina, ICSID Case No. ARB/03/9, Award, 5 September 2008, para. 258.

The *Total* tribunal similarly recalled the ‘powers’ as well as the ‘responsibility’ which BIT signatories have ‘to amend their legislation in order to adapt it to change and the emerging needs and requests of their people in the normal exercise of their prerogatives and duties’.<sup>158</sup> It added that ‘[t]his type of regulation [of a normative and administrative nature not specifically addressed to the relevant investor] is not shielded from subsequent changes under the applicable law’.<sup>159</sup>

The combination instituted by the arbitral tribunals in the first line of cases (*Occidental* or the early Argentine disputes) between the alleged requirement of stability and the legitimate expectations which are said to arise from the regulatory framework *per se*, should indeed be scrutinised with great caution. Generally, if any expectations, in such situations, are to arise at all, those are to the effect that sooner or later regulation will change over time, because ‘economic and legal life is by nature evolutionary’.<sup>160</sup> The crucial question becomes, indeed, the one of the right balance between the stability and legitimate expectations, on the one hand, and the host state’s right to amend the regulatory framework, on the other. This seems to be at the current focal point of debates as to the content of fair and equitable treatment.

If one attempts to piece together what emerges from the latest awards which have examined this topic, one can see that there has been a gradual limitation of the more far-reaching *dicta* found in the first generation cases seen above. The resulting framework can perhaps be delineated in the following terms.

First, to imply, without qualifications, a requirement of stability within fair and equitable treatment would place obligations on host states which would be ‘inappropriate and unrealistic’.<sup>161</sup> Preambular language which makes reference to a stable framework cannot suffice to establish such a burdensome obligation upon host states. For an investor to be legitimately able to claim damages as a result of the alteration of the general framework, additional guarantees are needed, such as an express contractual commitment (preferably in the form of stabilization clause) or a specific unilateral declaration attributable to the state that it would not proceed with changes.

Second, expectations as to the regulatory framework cannot be measured according to an abstract yardstick of good governance (which would be hard if not impossible to define), but must be assessed *in concreto*, with regard to all circumstances, including the specificities of the host state, its level of development, as well to the particular sector in which the investment is made.

These two different aspects will now be analysed in turn.

#### *a. Expectations of a stable framework v. specific commitments*

Arbitral tribunals taking a cautious approach as to the ability of instruments

<sup>158</sup> *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 115.

<sup>159</sup> *Id.*, para. 122 (however, adding a possible exception to this general rule, on which see *infra*).

<sup>160</sup> *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011, para. 352.

<sup>161</sup> *Saluka Investments BV v. The Czech Republic*, UNCITRAL-PCA, Partial Award, 17 March 2006, para. 304.

of general application (such as laws, regulations, etc.) to arouse legitimate expectations protected under the BIT have contrasted such situation with the scenario where the host state has assumed some form of *specific commitment* towards the investor. The idea behind this position is that if the state has renounced to exercise its regulatory power, this is such an extraordinary act that must emerge from an unequivocal commitment.<sup>162</sup> Such commitment can be for example in the form of a stabilization clause inserted in a state contract between the state and the investor.<sup>163</sup> Protection when a stabilization clause is present is higher because the investor has been able to bargain that commitment individually.<sup>164</sup> It would be thus illogical to extend such protection to investors who have not managed to bargain for such commitment (for whatever reason), by using the legitimate expectations doctrine.<sup>165</sup>

In *Parkerings v. Lithuania*, the tribunal contrasted the investor's alleged right to invoke a stable framework with a situation in which the investor is able to rely on a stabilization clause. It made the following general remark:

It is each State's undeniable right and privilege to exercise its sovereign legislative power. A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement, in the form of a *stabilisation* clause or otherwise, there is nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment.<sup>166</sup>

In *Continental*, the tribunal classified different types of state conduct that may allegedly generate expectations. It contrasted 'general legislative statements' to other types of undertakings (in particular contractual undertakings, which in the tribunal's opinion 'deserve clearly more scrutiny')<sup>167</sup> and found that general legislative statements only 'engender reduced expectations, especially with

<sup>162</sup> Suez et al. v. Argentina, ICSID Case No. ARB/03/17, Decision on Liability, 30 July 2010, Separate Opinion of Arbitrator Pedro Nikken, para. 31.

<sup>163</sup> In the definition given by the tribunal in *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 101, stabilization clauses are 'clauses, which are inserted in state contracts concluded between foreign investors and host states with the intended effect of freezing a specific host State's legal framework at a certain date, such that the adoption of any changes in the legal regulatory framework of the investment concerned (even by law of general application and without any discriminatory intent by the host State) would be illegal'.

<sup>164</sup> See also Sergei Paushok, *Cjsc Golden East Company, Cjsc Vostokneftegaz Company v. Mongolia*, UNCITRAL, Award on Jurisdiction and Liability, 28 April 2011, para. 302 ('foreign investors are acutely aware that significant modification of taxation levels represents a serious risk, especially when investing in a country at an early stage of economic and institutional development. In many instances, they will obtain the appropriate guarantees in that regard in the form of, for example, stability agreements which limit or prohibit the possibility of tax increases. [...] In the absence of such a stability agreement in favor of GEM, Claimants have not succeeded in establishing that they had legitimate expectations that they would not be exposed to significant tax increases in the future').

<sup>165</sup> See Elizabeth Snodgrass, *Protecting Investors' Legitimate Expectations – Recognizing and Delimiting a General Principle*, 21 ICSID REV. - FOREIGN INV. L.J. 1, 38 (2006).

<sup>166</sup> *Parkerings-Compagniet AS v. Lithuania*, ICSID Case No. ARB/05/8, Award, 11 September 2007, para. 332 (emphasis in the original).

<sup>167</sup> *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9, Award, 5 September 2008, para. 261.

competent major international investors in a context where the political risk is high. Their enactment is by nature subject to subsequent modification, and possibly to withdrawal and cancellation, within the limits of respect of fundamental human rights and *ius cogens*.<sup>168</sup>

Also the tribunal in *Total* noted that the legal regime in force at the time of making the investment is not *per se* subject to a guarantee of stability, unless the state has explicitly assumed a legal obligation such as a stabilization clause.<sup>169</sup> The tribunal also contrasted the (unfounded) right to stability with the situation where the claimant was able to rely on a unilateral declaration by the host state (which the claimant was not, in the case at hand).<sup>170</sup> Thus, in agreement with *Continental*, also *Total* suggests that the general framework only engenders those ‘reduced’ expectations, which enjoy the weakest form of protection if compared to contractual commitments and specific promises. Reduced protection of statements or guarantees contained in legislation is justified because these ‘promises’ are not addressed to individual subjects (i.e., they lack the element of specificity with regard to the addressee).<sup>171</sup> The findings in *EDF v. Romania*<sup>172</sup> and *El Paso v. Argentina*<sup>173</sup> are to a similar effect.<sup>174</sup>

The most difficult question is whether there can be instances where the change in regulatory framework is so severe or radical that, even in the absence of a stabilization clause or an individualised representation, a tribunal may nonetheless find a violation of the fair and equitable treatment by reference to a frustration of the investor’s legitimate expectations. It is interesting to note that even tribunals which showed great caution on this issue, such as *Total* and *El Paso*, did not go as far as ruling out completely that possibility.

In *El Paso* the tribunal made the following statement:

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<sup>168</sup> *Id.*

<sup>169</sup> *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, paras. 117, 429.

<sup>170</sup> *Id.*, paras. 118-124.

<sup>171</sup> *Id.*, paras. 121-124.

<sup>172</sup> *EDF (Services) Limited v. Romania*, ICSID Case No. ARB/05/13, Award, 8 October 2009, para. 217 (‘The idea that legitimate expectations, and therefore FET, imply the stability of the legal and business framework, may not be correct if stated in an overly-broad and unqualified formulation. The FET might then mean the virtual freezing of the legal regulation of economic activities, in contrast with the State’s normal regulatory power and the evolutionary character of economic life. Except where specific promises or representations are made by the State to the investor, the latter may not rely on a bilateral investment treaty as a kind of insurance policy against the risk of any changes in the host State’s legal and economic framework. Such expectation would be neither legitimate nor reasonable’).

<sup>173</sup> *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011, paras. 364 (‘the legitimate expectations of a foreign investor can only be examined by having due regard to the general proposition that the State should not unreasonably modify the legal framework or modify it in contradiction with a specific commitment not to do so’, emphasis omitted) and 368 (‘FET cannot be designed to ensure the immutability of the legal order, the economic world and the social universe and play the role assumed by stabilisation clauses specifically granted to foreign investors with whom the State has signed investment agreements’).

<sup>174</sup> See also *EnCana Corporation v. Ecuador*, UNCITRAL/LCIA Case No. UN 3481, Award, 3 February 2006 (‘In the absence of a specific commitment from the host State, the foreign investor has neither the right nor any legitimate expectation that the tax regime will not change, perhaps to its disadvantage, during the period of the investment’, internal footnote omitted).

There can be no legitimate expectation for anyone that the legal framework will remain unchanged in the face of an extremely severe economic crisis. No reasonable investor can have such an expectation unless very specific commitments have been made towards it or *unless the alteration of the legal framework is total*.<sup>175</sup>

The tribunal did not further explain what it would take for an alteration of the framework to be ‘total’. It possibly found a way out of this conundrum, by holding that the several measures at issue which altered the framework did not constitute a violation of the BIT, if taken *in isolation*, but did so, if their *cumulative effect* was combined. The tribunal observed that:

It cannot be denied that in the matter before this Tribunal the cumulative effect of the measures was a total alteration of the entire legal setup for foreign investments, and that all the different elements and guarantees just mentioned can be analysed as a special commitment of Argentina that such a total alteration would not take place.<sup>176</sup>

It has been seen that *Total* also stands for the proposition that, in principle, absent a stabilization clause or a unilateral individualised representation, there can be no legitimate claim of frustration of expectations arising from the regulatory framework *per se*. Yet, the tribunal was not willing to consider this as an absolute rule subject to no exceptions. After stating that instruments of general regulation are not shielded from subsequent changes under the applicable law, the tribunal introduced an exception:

This notwithstanding, a claim to stability can be based on the inherently prospective nature of the regulation at issue aimed at providing a defined framework for future operations. This is the case for regimes, which are applicable to long-term investments and operations, and/or providing for “fall backs” or contingent rights in case the relevant framework would be changed in unforeseen circumstances or in case certain listed events materialize.<sup>177</sup>

It held that according to the gas regime which Argentina had enacted, the state was empowered to fix the tariffs of a public utility, but it had to do so ‘in such a way that the concessionaire [was] able to recover its operations costs, amortize its investments and make a reasonable return over time’.<sup>178</sup> The tribunal found that the failure to readjust the tariffs according to principles of ‘economic equilibrium and business viability’ entailed a violation of the fair and equitable treatment.<sup>179</sup> Similar considerations were then repeated with regard to the different claims relating to the electricity sector.<sup>180</sup> In perhaps even clearer terms,

<sup>175</sup> El Paso Energy International Company v. Argentina, ICSID Case No. ARB/03/15, Award, 31 October 2011, para. 274.

<sup>176</sup> *Id.*, para. 517.

<sup>177</sup> Total S.A. v. Argentina, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 112.

<sup>178</sup> *Id.*

<sup>179</sup> *Id.*, paras. 166-175, and esp. 168.

<sup>180</sup> *Id.*, para. 313.



the arbitral tribunal found that

Expectations based on [principles of economic rationality, public interest, reasonableness and proportionality] are reasonable and hence legitimate, *even in the absence of specific promises by the government*. Hence, the fair and equitable standard has been breached through the setting of prices that do not remunerate the investment made nor allow reasonable profit to be gained contrary to the principles governing the activities of privately owned generators under Argentina's own legal system.<sup>181</sup>

As already mentioned, the *Parkerings* tribunal held that, absent a specific promise by the host state, a claim of stability of the framework could not be justified. It concluded by saying that:

The record does not show that the State acted unfairly, unreasonably or inequitably in the exercise of its legislative power. The Claimant has failed to demonstrate that the modifications of laws were made *specifically to prejudice its investment*.<sup>182</sup>

Thus, the tribunal seemed to suggest that it will be relevant to look at whether the legislative modifications at issue evinced a form of prejudicial intent against the investor (in which case one can assume the tribunal would have been ready to find a breach of the BIT).

In *PSEG v. Turkey*, the tribunal held that 'stability cannot exist in a situation where the law kept changing continuously and endlessly, as did its interpretation and implementation.'<sup>183</sup> Thus, unlike *El Paso*, where the focus was on the *totality* of the change, here the tribunal found the violation to have occurred as a result of what it called the 'roller-coaster' effect of the regulatory modifications.<sup>184</sup>

In *Toto v. Lebanon*, the tribunal found no liability on the part of the respondent. It held that:

In the absence of a stabilisation clause or similar commitment, which were not granted in the present case, changes in the regulatory framework would be considered as breaches of the duty to grant full protection and fair and equitable treatment *only in case of a drastic or discriminatory change* in the essential features of the transaction.<sup>185</sup>

And in *Impregilo v. Argentina*, the tribunal set out the following test:

The legitimate expectations of foreign investors cannot be that the State will never modify the legal framework, especially in times of crisis, but

<sup>181</sup> *Id.*, para. 333 (emphasis added).

<sup>182</sup> *Parkerings-Compagniet AS v. Lithuania*, ICSID Case No. ARB/05/8, Award, 11 September 2007, para. 337 (emphasis added).

<sup>183</sup> *PSEG v. Turkey*, ICSID Case No. ARB/02/5, Award, 19 January 2007, para. 254.

<sup>184</sup> *Id.*, para. 250.

<sup>185</sup> *Toto Construzioni Generali S.p.A. v. Lebanon*, ICSID Case No. ARB/07/12, Award, 7 June 2012, para. 244.

certainly investors must be protected from *unreasonable* modifications of that legal framework.<sup>186</sup>

As one can see by looking at all these pronouncements, there is no single answer to the question as to when a change of regulatory framework (absent a specific commitment) would entail a violation of the fair and equitable treatment. The tests proposed by the tribunals vary, ranging from consideration of the extent of the change (*El Paso*), to the way change occurs (*PSEG*), up to the discriminatory effect (*Toto* and *Parkerings*) or the unreasonable nature (*Impregilo*) of such change. The impression one receives is that in some instances the legal test was dictated by the specific facts of the case (and possibly also the different industry sectors at stake). Perhaps a definition of the exact (and abstract) threshold that would be applicable in all types of situations is an impossible endeavour. Some may view this as regrettable for the ensuing lack of legal certainty, with stakeholders left in the unpredictability as to when a change in framework will cross the line and become a treaty breach. One may, however, envisage certain general safeguards that states should observe in order to avoid liability under a BIT when a significant change of the regulatory framework is susceptible to impact on foreign investors. For example, in order for the change not to be too abrupt, the host state should give those affected by the change adequate warning, and, where possible, adopt transitional measures.<sup>187</sup> It is to be expected that the presence of such safeguards will be taken into account by an arbitral tribunal when deciding whether a breach of fair and equitable treatment has occurred.

*b. Expectations must take into account all circumstances, including the level of development of the host country*

A second field where the tribunals' analysis has become more refined in the recent years has concerned the more precise content that investors' expectations assume (or should assume) vis-à-vis a certain regulatory framework, which is later modified. Tribunals have generally stressed that expectations need to be 'reasonable' in order to attract protection under the fair and equitable treatment standard.<sup>188</sup> But what are the factors that an arbitral tribunal should consider when

<sup>186</sup> *Impregilo S.p.A. v. Argentina*, ICSID Case No. ARB/07/17, Final Award, 21 June 2011, para. 291 (emphasis added).

<sup>187</sup> See, e.g., *CNTA SA v. Commission*, Case 74/74, 14 May 1975 [1975] E.C.R. 533, paras. 42-44 (where the ECJ held that the Community was liable in damage if, in the absence of an overriding public interest, the Commission abolished certain monetary compensation amounts without adopting transitional measures that would have enabled the traders either to have avoided the loss suffered in the performance of the export contracts or to be compensated for such loss).

<sup>188</sup> The term 'reasonable' has either been used as a synonym to 'legitimate' or to denote an additional feature that 'legitimate' expectations must meet. See, e.g., *International Thunderbird Gaming Corporation v. Mexico*, NAFTA/UNCITRAL, Award, 26 January 2006, para. 147 (defining legitimate expectations as 'reasonable and justifiable expectations'); *Jan de Nul N.V. and Dredging International N.V. v. Egypt*, ICSID Case No. ARB/04/13, Award, 6 November 2008, para. 186 ('reasonable and legitimate' expectations); *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9, Award, 5 September 2008, para. 260 ('reasonable legitimate expectations'); *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 333 ('reasonable and hence legitimate' expectations);

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assessing the degree of reasonableness of the expectations (and therefore their ultimate legitimacy)?

Tribunals have observed that the investor's legitimate expectations have to be put into relation with the host state's specific characteristics in terms of investment environment. It would seem quite obvious that what an investor can legitimately expect (especially in terms of level of stability or transparency) cannot be the same in a highly developed country as it is in a developing or emerging economy. One treaty, the Investment Agreement for the Common Market for Eastern and Southern Africa (COMESA) Common Investment Area, introduces in its text an element of flexibility in the interpretation of the fair and equitable treatment standard precisely based on the level of development of the respondent country.<sup>189</sup>

Even in the absence of such an express reference in the text of the treaty, arbitral tribunals have been ready to consider that the reasonableness requirement inherent in expectations allows for, or even mandates, an examination of all circumstances that the investor should have considered when making the investment, including the level of development of the host country.<sup>190</sup>

In *Duke v. Ecuador*, the tribunal set out a holistic approach to the evaluation of expectations:

The assessment of the reasonableness or legitimacy [of the investor's expectations] must take into account all circumstances, including not only the facts surrounding the investment, but also the political, socioeconomic, cultural and historical conditions prevailing in the host State.<sup>191</sup>

Account for contextualisation is also present in other awards which deal with legitimate expectations.<sup>192</sup> In *Bayindir v. Pakistan*, the tribunal found that the investor had made its investment with the full knowledge of an investment climate affected by high 'political volatility'.<sup>193</sup> Thus, claimant could not rely on 'wider expectations of stability and predictability so as to justify protection under the FET standard'.<sup>194</sup>

In *Toto v. Lebanon*, according to the arbitral tribunal, 'the post-civil war

Grand River Enterprises Six Nations Ltd et al. v. USA, NAFTA/UNCITRAL, Award, 12 January 2011, paras. 140, 141 ('reasonable or legitimate expectations').

<sup>189</sup> See Investment Agreement for the COMESA Common Investment Area (2007), Art. 14(3) ('For greater certainty, Member States understand that different Member States have different forms of administrative, legislative and judicial systems and that Member States at different levels of development may not achieve the same standards at the same time. Paragraphs 1 and 2 of this Article [prohibition of denial of justice and affirmation of the minimum standard of treatment of aliens] do not establish a single international standard in this context').

<sup>190</sup> See Ursula Kriebaum, *The Relevance of Economic and Political Conditions for Protection under Investment Treaties*, 10 THE LAW AND PRACTICE OF INTERNATIONAL COURTS AND TRIBUNALS 383 (2011).

<sup>191</sup> *Duke Energy Electroquil Partners and Electroquil SA v. Ecuador*, ICSID Case No. ARB/04/19, Award, 12 August 2008, para. 340.

<sup>192</sup> See, in addition to the awards discussed *infra*, *Genin et al. v. Estonia*, ICSID Case No. ARB/99/2, Award, 25 June 2001, para. 348; *Nagel v. Czech Republic*, SCC No. 049/2002, Award, 9 September 2003, para. 293.

<sup>193</sup> *Bayindir Insaat Turizm Ticaret Ve Sanayi A.Ş. v. Pakistan*, ICSID Case No. ARB/03/29, Award, 27 August 2009, para. 195.

<sup>194</sup> *Id.*, para. 194.

situation in Lebanon, with substantial economic challenges and colossal reconstruction efforts, did not justify legal expectations that custom duties would remain unchanged'.<sup>195</sup>

In many circumstances, an investor may be attracted to invest in a developing country because the possibility of earning a rate of return on its capital may be higher than in developed economies.<sup>196</sup> Yet, the presumably greater instability will be indeed part of the business risk, and an inquiry into the reasonableness of its expectations should not fail to assess this element.<sup>197</sup> In *Parkerings v. Lithuania*, for example, the tribunal expressly noted that circumstances in a country in transition could not justify legitimate expectation as regards the stability of the investment environment. A prudent businessman would have sought to protect its legitimate expectations through a stabilization clause.<sup>198</sup>

Finally, risk connected to a developing country's economic situation is not the only risk the investor must assess. In a developed economy, an investor must realistically assess regulatory risk.<sup>199</sup> Thus, in *Methanex v. USA*, the tribunal held that the investor could not have expected that California would refrain from regulatory changes. The investor had knowingly entered a framework in which there was close supervision from various interest groups and the concern for environmental issues was notoriously high.<sup>200</sup> Similarly, in *Glamis Gold v. USA*, the claim of frustration of legitimate expectations failed, partly because 'Claimant was operating in a climate that was becoming more and more sensitive to the environmental consequences of open-pit mining'.<sup>201</sup>

<sup>195</sup> *Toto Construzioni Generali S.p.A. v. Lebanon*, ICSID Case No. ARB/07/12, Award, 7 June 2012, para. 245.

<sup>196</sup> See *Generation Ukraine, Inc. v. Ukraine*, ICSID Case No. ARB/00/9, Award, 16 September 2003, para. 20.37 (noting that 'it is relevant to consider the vicissitudes of the economy of the state that is host to the investment in determining the investor's legitimate expectations, the protection of which is a major concern of the minimum standards of treatment contained in bilateral investment treaties. The Claimant was attracted to the Ukraine because of the possibility of earning a rate of return on its capital in significant excess to the other investment opportunities in more developed economies').

<sup>197</sup> See also *LG&E Energy Corp et al. v. Argentina*, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006 (noting that 'the investor's fair expectations cannot fail to consider parameters such as business risk or industry's regulatory patterns'). See also the more general observation, made by the tribunal in *Maffezini*, and quoted with approval by several subsequent tribunals, that 'Bilateral Investment Treaties are not insurance policies against bad business judgments'. See *Maffezini v. Spain*, ICSID Case No. ARB/97/7, Award on the Merits, 13 November 2000, para. 64; *CMS Gas Transmission Company v. Argentina*, ICSID Case No. ARB/01/08, Decision of the Tribunal on Objections to Jurisdiction, 17 July 2003, para. 29; *Waste Management, Inc. v. Mexico*, ICSID Case No. ARB(AF)/00/3, Award, 30 April 2004, para. 114; *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Chile*, ICSID Case No. ARB/01/7, Award, 25 May 2004, para. 178; *EDF (Services) Limited v. Romania*, ICSID Case No. ARB/05/13, Award, 8 October 2009, para. 217; *Total S.A. v. Argentina*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010, para. 124.

<sup>198</sup> *Parkerings-Compagniet AS v. Lithuania*, ICSID Case No. ARB/05/8, Award, 11 September 2007, paras. 335-336.

<sup>199</sup> See Meg Kinnear, *The Continuing Development of the Fair and Equitable Treatment Standard*, in *INVESTMENT TREATY LAW: CURRENT ISSUES III* 209, 233 (Andrea K. Bjorklund, Ian A. Laird, & Sergey Ripinsky eds., 2009).

<sup>200</sup> *Methanex Corporation v. USA*, NAFTA/UNCITRAL, Final Award of the Tribunal on Jurisdiction and Merits, 3 August 2005, Part IV – Ch. D, paras. 9-10 (remarks made when discussing expropriation).

<sup>201</sup> *Glamis Gold, Ltd. v. USA*, NAFTA/UNCITRAL, Award, 8 June 2009, para. 767.

### 3. Assessing the ‘reasonableness’ of the expectation: the investor’s conduct

It has been seen that consideration for socio-economic circumstances helps shaping the content of expectations. The reasonableness requirement inherent in expectations is in turn affected by a further component, which concerns the role played the investor in the investment operation.<sup>202</sup> This again means that expectations have to be analysed *in concreto* in order to determine whether the investor has acted with diligence and thus can be said to hold the expectations in the relevant circumstances. The investor’s diligent conduct comes into play irrespective of the source that arouses the expectation, i.e., regardless of whether the expectation is rooted in a contractual commitment, in a unilateral representation, or in the regulatory framework. A few examples will illustrate the point.

In *ADF v. USA*, one of the first cases to make reference to the concept of legitimate expectations (although without in-depth explanation),<sup>203</sup> the tribunal discussed the investor’s expectation allegedly created by existing case-law. It denied the existence of a legitimate expectation because the expectation was not created by ‘any misleading representations made by authorized officials of the US federal government but rather...by legal advice received from private counsel’.<sup>204</sup> If the investor knows (or ought to have known, by acquiring proper legal advice) that it cannot attain a certain result or act, because that would contravene the host state’s domestic law, a legitimate expectation cannot be said to have arisen. It is useful to return to the already seen *MTD v. Chile* case. The tribunal found that the Chilean government had created expectations by supporting the real estate project by, *inter alia*, entering into the investment contract. However, the laws in force did not permit the land the investor had acquired to be developed for commercial purposes. Further, the investment contract between the two parties made the approval in question subject to other necessary authorizations, and merely assented to the transfer of foreign capital flows to Chile. The finding of legitimate expectations is questionable in these circumstances. If the investor had performed a diligent inquiry into the regulatory framework, it could not have developed legitimate expectations at all in the first place, because its investigation would have evinced that his investment could not proceed as planned.<sup>205</sup> Yet, the tribunal decided that it was justified to protect the investor’s expectations under the fair and equitable treatment standard, because the government had not been clear in dealing with the claimant. However, in a Solomonic decision, the tribunal reduced

<sup>202</sup> See Peter Muchlinsky, ‘*Caveat Investor*’? *The relevance of the conduct of the investor under the fair and equitable treatment standard*, 55 ICLQ 527 (2006) (analysing the relevance of the investor’s conduct under fair and equitable treatment, and finding that investors have mainly three duties: to refrain from unconscionable conduct, to engage in the investment in the light of an adequate knowledge of its risks, and to conduct business in a reasonable manner).

<sup>203</sup> See *supra* note 66.

<sup>204</sup> *ADF Group v. USA*, ICSID Case No. ARB(AF)/00/1, Award, 9 January 2003, para. 189.

<sup>205</sup> But see Elizabeth Snodgrass, *Protecting Investors’ Legitimate Expectations – Recognizing and Delimiting a General Principle*, 21 ICSID REV. - FOREIGN INV. L.J. 1, 40 (2006) (‘the compliance or non-compliance with municipal law of an administrative act that gave rise to expectations should not be determinative of the degree of protection, if any, those expectations will receive in international law’).



by 50 per cent the damages awarded based on the fact that the investor should have made an independent assessment.<sup>206</sup>

In *Metalpar v. Argentina*, the tribunal observed that the investor had relevant business experience and knowledge that the automobile industry in Argentina was in bad conditions. This convinced the tribunal that it was ‘unlikely that Claimants legitimately expected that their investments would not be subject to the ups and downs of the country in which they were made or that the crisis that could already be foreseen would not make it necessary to issue legal measures to cope with it’.<sup>207</sup> It thus found that no violation of the fair and equitable treatment had occurred.

It is quite evident that legitimate expectations are unworthy of protection if the representation, promise, or assurance was procured by fraud, or if the investor failed to disclose relevant facts. The latter situation occurred in *Thunderbird v. Mexico*. Amongst the reasons that convinced the majority that the claimant could not have any legitimate expectations was that in its submission to a governmental authority the investor had not supplied adequate information and made a proper disclosure.<sup>208</sup> Similarly, in *Chemtura v. Canada* the tribunal found that ‘the disingenuous position taken by the Claimant’ could not ‘justify a “reasonable” or “legitimate” expectation’.<sup>209</sup>

## V. Concluding remarks

Legitimate expectations have penetrated investment treaty jurisprudence of the last decade in a pervasive way. This paper has first attempted to provide a description of the roots of the concept. It has looked at national administrative law systems, as well as at the EU framework, with a view to grasping the common features of protection of expectations under those systems. While differences between each system are inevitable, core similarities could be highlighted. This is particularly important if one attempts to inform the content of ‘fair and equitable treatment’ under investment treaties by way of reference to principles of law as embodied in the principal legal systems of the world.

In the investment treaty context, first generation awards display an almost complete lack of analysis as to the reasons for including protection of legitimate expectations as a sub-element, or indeed the ‘dominant’ sub-element, of fair and equitable treatment. Later and more recent awards, while building on the established line of earlier cases, are commendable for providing a fine-tuning of many of the issues involved in the doctrine of legitimate expectations. This paper has attempted to group the situations where expectations are typically invoked, by looking at the different conduct by the host state. Thus, when a contractual commitment is at stake, the expectation factor appears to be the strongest. Yet, it has also been seen that resort to this concept in this situation entails the risk of equating any kind of contractual expectation with a genuine treaty claim.

In a second type of situation, the concept of legitimate expectations is particularly useful to describe a situation where the host state has induced an

<sup>206</sup> MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Chile, ICSID Case. No. ARB/01/7, Award, 25 May 2004, paras. 168-178, 242-246.

<sup>207</sup> Metalpar S.A. and Buen Aire S.A. v. Argentina, ICSID Case ARB/03/05, Award on the Merits, 6 June 2008, para. 187.

<sup>208</sup> International Thunderbird Gaming Corporation v. Mexico, NAFTA/UNCITRAL, Award, 26 January 2006, paras. 151-159.

<sup>209</sup> Chemtura Corporation v. Canada, NAFTA/UNCITRAL, Award, 2 August 2010, para. 179.

investment by way of certain informal representations or promises, on which the investor has relied at the time of making the investment. If these are both specific and individualised, the doctrine of legitimate expectations will provide a valuable tool to hold the host state liable. This approach is in line with domestic law systems which typically extend protection to legitimate expectations in these kinds of situations. It would also be in line with public international law rules on unilateral acts, to the extent that those were to be considered applicable by analogy in investor-state relations.

Finally, the paper has addressed the situation where the claimant alleges that its expectations are tied to a stable regulatory framework. In those circumstances the use of legitimate expectations cannot be easily justified, unless strict limits are posed. Two areas have in particular seen a refinement in the tribunals' analysis. First, what an investor may expect has to be assessed according to the totality of circumstances, including the socio-economic situation and the development level of the host state. Second, the investor's own conduct plays a crucial role in evaluating whether the expectation was reasonable, and hence legitimate, in those set of circumstances. Meg Kinnear has rightly asked whether account for this variables (the investor's conduct, the reasonableness of the investor's expectations, or the level of the development of the host state) does not undermine one of the most basic premises underlying fair and equitable treatment, i.e., its absolute (non-relative) nature.<sup>210</sup> Yet, this seems almost an inevitable consequence of resorting to a concept, the 'expectation', that bears a certain level of subjectivity.<sup>211</sup> But at the same time the idea of legitimate expectations is an extremely flexible tool that allows arbitral tribunals to balance investors' interests and the host state's right to regulate,<sup>212</sup> in line with the more general balancing idea behind fair and equitable treatment.<sup>213</sup> Arbitral tribunals will no doubt continue to provide clearer guidance to such balancing exercise and to contribute

<sup>210</sup> Meg Kinnear, *The Continuing Development of the Fair and Equitable Treatment Standard*, in INVESTMENT TREATY LAW: CURRENT ISSUES III 209, 236 (Andrea K. Bjorklund, Ian A. Laird, & Sergey Ripinsky eds., 2009).

<sup>211</sup> See Emmanuel Gaillard, *CIRDI, Chronique de sentences arbitrales*, JOURNAL DE DROIT INTERNATIONAL 332 (2008) (warning against the 'exacerbated subjectivism' associated with legitimate expectations).

<sup>212</sup> See, e.g., *Saluka Investments BV v. The Czech Republic*, UNCITRAL-PCA, Partial Award, 17 March 2006, paras. 304-306, 306 (the determination of a breach of fair and equitable treatment 'requires a weighing of the Claimant's legitimate and reasonable expectations on the one hand and the Respondent's legitimate regulatory interests on the other'); *International Thunderbird Gaming Corporation v. Mexico*, NAFTA/UNCITRAL, Award, 26 January 2006, Separate Opinion Thomas Wälde, para. 30 (the doctrine entails a 'balancing process between the needs for flexible public policy and the legitimate reliance on in particular investment-backed expectations'); *El Paso Energy International Company v. Argentina*, ICSID Case No. ARB/03/15, Award, 31 October 2011, para. 356 ('the notion of "legitimate expectations" is an objective concept, that it is the result of a balancing of interests and rights'); *Toto Construzioni Generali S.p.A. v. Lebanon*, ICSID Case No. ARB/07/12, Award, 7 June 2012, para. 165 (recognition of legitimate expectations 'is the result of a balancing operation of the different interests at stake, taking into account all circumstances, including the political and socioeconomic conditions prevailing in the host State').

<sup>213</sup> See, e.g., CAMPBELL MCLACHLAN, LAURENCE SHORE & MATTHEW WEINIGER, INTERNATIONAL INVESTMENT ARBITRATION. SUBSTANTIVE PRINCIPLES 239 (2007) (noting the 'more general notion of balance between the interests of the investor and the countervailing factor of the State acting in the public interest' which is 'inherent in the concept of "equitable treatment"').

to a more precise standard of review that should be utilized in this respect.<sup>214</sup> It is, however, evident that case law has already gone a long way from an early utilisation of the concept of legitimate expectations as a rhetorical and potentially boundless catchphrase, towards a more coherent and rigorous application of the doctrine, which is wary of its limitations.

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<sup>214</sup> See Caroline Henckels, *Proportionality and the Standard of Review in Fair and Equitable Treatment Claims: Balancing Stability and Consistency with the Public Interest*, SIEL Working Paper No. 2012/27, 26 June 2012, available at <http://ssrn.com/abstract=2091474>.